Legislative Proposals and Explanatory Notes on Taxation of Non-Resident Trusts and Foreign Investment Entities

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The Honourable Paul Martin, P.C., M.P.
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For additional copies of this document
please contact:

Distribution Centre
Department of Finance
300 Laurier Avenue West
Ottawa K1A 0G5

Tel: (613) 995-2855
Fax: (613) 996-0518

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Legislative Proposals

1. (1) Paragraph 12(1)(*k*) of the *Income Tax Act* is replaced by the following:

Foreign corporations, trusts and investment entities

(*k*) any amount required by subdivision i to be included in computing the taxpayer's income for the year;

(2) Subsection (1) applies to taxation years that begin after 2000.

2. (1) The definition "controlled foreign affiliate" in subsection 17(15) of the Act is replaced by the following:

"controlled foreign affiliate"
« société étrangère affiliée contrôlée »

"controlled foreign affiliate" has the meaning that would be assigned by the definition "controlled foreign affiliate" in subsection 95(1) if this Act were read without reference to subsection 94.1(12) and if paragraphs (*d*) and (*e*) of that definition read as follows:

"(*d*) one or more persons resident in Canada with whom the taxpayer does not deal at arm's length, or

(*e*) the taxpayer and one or more persons resident in Canada with whom the taxpayer does not deal at arm's length."

(2) Subsection (1) applies after 2000.

3. (1) Paragraph 39(1)(*a*) of the Act is amended by adding the following after subparagraph (ii.2):

(ii.3) a property in respect of which subsection 94.2(3) applies to the taxpayer immediately before the time of the disposition,

(2) Subsection (1) applies to dispositions that occur after 2000.

4. (1) Paragraph 53(1)(*d*.1) of the Act is replaced by the following:

(*d*.1) where the property is a capital interest of the taxpayer in a trust to which paragraph 94(1)(*d*) applied (as that paragraph read in its application before 2001), any amount required by paragraph 94(5)(*a*) (as that paragraph read in its application before 2001) to be added in computing the adjusted cost base to the taxpayer of the interest;

(2) Paragraph 53(1)(*m*) of the Act is replaced by the following:

(*m*) where the property is an offshore investment fund property (within the meaning assigned by subsection 94.1(1) as that subsection read in its application before 2001),

(i) any amount included in respect of the property under subsection 94.1(1) (as that subsection read in its application before 2001) in computing the taxpayer's income for a taxation year that began both before that time and before 2001, and

(ii) where the taxpayer is a controlled foreign affiliate of a person resident in Canada, any amount included in respect of the property in computing the foreign accrual property income of the controlled foreign affiliate because of the description of C in the definition "foreign accrual property income" in subsection 95(1) for a taxation year of the controlled foreign affiliate that began both before that time and before 2001;

(*m*.1) any amount required by subsection 94.1(9) or 94.2(11) to be added at or before that time in computing the adjusted cost base to the taxpayer of the property;

(3) Subsection 53(2) of the Act is amended by striking out the word "and" at the end of paragraph (*u*), by adding the word "and" at the end of paragraph (*v*) and by adding the following after paragraph (*v*):

(*w*) any amount required by subsection 94.1(9), 94.2(11) or 94.3(2) to be deducted at or before that time in computing the adjusted cost base to the taxpayer of the property.

(4) Subsections (1) to (3) apply after 2000.

5. (1) Subsection 70(3.1) of the Act is replaced by the following:

Exception

(3.1) For the purposes of this section, "rights or things" in respect of an individual do not include an interest in a life insurance policy (other than an annuity contract where the payment for the contract was deductible in computing the individual's income under paragraph 60(*l*) or was made in circumstances in which subsection 146(21) applied), eligible capital property, land included in the inventory of a business, a Canadian resource property, a foreign resource property or property in respect of which subsection 94.2(3) applied to the individual immediately before the individual's death.

(2) Subsection 70(5.2) of the Act is amended by striking out the word "and" at the end of paragraph (*c*), by adding the word "and" at the end of paragraph (*d*) and by adding the following after paragraph (*d*):

(*e*) where subsection 94.2(3) applies to the taxpayer in respect of the property immediately before the taxpayer's death,

(i) the taxpayer is deemed to have disposed of the property at that time for proceeds equal to the fair market value of the property at that time,

(ii) for the purposes of subsection 94.2(4), the taxpayer is deemed not to hold the property after that time, and

(iii) any person who acquires the property as a consequence of the taxpayer's death is deemed to acquire the property at the time of the taxpayer's death at a cost equal to the proceeds referred to in subparagraph (i).

(3) Subsections (1) and (2) apply to the 2001 and subsequent taxation years.

6. (1) Subsection 75(3) of the Act is amended by striking out the word "or" at the end of paragraph (*c*.1) and by adding the following after paragraph (*c*.1):

(*c*.2) by a trust that is non-resident for the purposes of computing its income for the year, notwithstanding that there is a person who is, at the end of the year, both resident in Canada and a contributor (as defined in section 94) to the trust; or

(2) Subsection (1) applies to trust taxation years that begin after 2000.

7. (1) Paragraph 85(1.1)(*g*) of the Act is amended by striking out the word "or" at the end of subparagraph (ii) and by adding the following after subparagraph (ii):

(ii.1) a property held by the taxpayer if subsection 94.2(3) applies to the taxpayer in respect of the property, or

(2) Subsection (1) applies after 2000.

8. (1) Subsection 87(2) of the Act is amended by adding the following after paragraph (*j*.94):

Non-resident trusts and foreign investment entities

(*j*.95) for the purposes of sections 94 to 94.3, the new corporation is deemed to be the same corporation as, and a continuation of, each predecessor corporation;

(2) Subsection (1) applies after 2000.

9. (1) Subsection 91(1) of the Act is replaced by the following:

Amounts to be included in respect of share of foreign affiliate

91. (1) In computing the income for a taxation year of a taxpayer resident in Canada, there shall be included, in respect of each share owned by the taxpayer of the capital stock of a controlled foreign affiliate of the taxpayer, as income from the share, the percentage of the foreign accrual property income of any controlled foreign affiliate of the taxpayer, for each taxation year of the affiliate that ends in the taxation year of the taxpayer, equal to the amount that would be that share's participating percentage in respect of the affiliate, determined at the end of each such taxation year of the affiliate if paragraph (*a*) of the definition "equity percentage" in subsection 95(4) did not take into account each share that would be subject to subsection 94.2(9) in respect of the taxpayer for the year if the taxpayer held the share throughout the year.

(2) Subparagraph 91(4)(*a*)(ii) of the Act is replaced by the following:

(ii) the taxpayer's relevant tax factor for the year, and

(3) Subsection (1) applies to taxation years that begin after 2000.

(4) Subsection (2) applies after 2000.

10. (1) Section 94 of the Act is replaced by the following:

Treatment of Trusts with Canadian Contributors

Definitions

94. (1) The definitions in this subsection apply in this section.

"accounting profit"
« bénéfices comptables »

"accounting profit" of a trust for a taxation year of the trust means

(*a*) where the trust prepares financial statements in accordance with accounting principles substantially similar to generally accepted accounting principles used in Canada, the trust's profit for the year (determined before taking into account income or profits tax) reflected in the trust's financial statements; and

(*b*) in any other case, the amount that would be the trust's total profit for the year (determined before taking into account income or profits tax) from businesses carried on by the trust, properties owned by the trust, or any combination of those businesses and properties, if that amount were calculated in accordance with generally accepted accounting principles used in Canada.

"arm's length transfer"
« transfert sans lien de dépendance »

"arm's length transfer" at any time by a person or partnership (in this definition referred to as the "transferor") in respect of a trust means a particular transfer or loan of property at that time by the transferor to a particular person or partnership (in this definition referred to as the "recipient") where

(*a*) one of the following applies, namely,

(i) in exchange for the particular transfer or loan, the recipient transfers or loans property, or becomes obligated to transfer or loan property, and it is reasonable to conclude, having regard only to the particular transfer or loan and the property transferred or loaned, or obligated to be transferred or loaned, by the recipient to the transferor in exchange, that

(A) the exchange is one that the transferor would have been willing to carry out if the transferor had dealt at arm's length with the recipient, and

(B) the terms and conditions made or imposed in respect of the exchange would have been acceptable to the transferor if the transferor had dealt at arm's length with the recipient,

(ii) the particular transfer or loan is a payment of interest, a dividend, rent, a royalty or any similar return on investment, or any substitute for such a return on investment, in respect of a particular property owned by the recipient immediately before that time, if the fair market value at that time of the property so transferred does not exceed the fair market value of property that the transferor would have been willing to transfer at that time in respect of the particular property to the recipient if the transferor had dealt at arm's length with the recipient,

(iii) the particular transfer or loan

(A) is in satisfaction of an obligation that arose because of a transfer to which subparagraph (i) applied, and

(B) is one that the transferor would have been willing to carry out if the transferor had dealt at arm's length with the recipient,

(iv) the particular transfer or loan was made in the ordinary course of the business of the transferor, or

(v) it is reasonable to conclude that none of the reasons for the particular transfer or loan was to permit or facilitate, directly or indirectly, the conferral, in the future, of a benefit in respect of the trust on

(A) the transferor,

(B) a descendant of the transferor, or

(C) any person with whom the transferor or descendant does not deal at arm's length; and

(*b*) it is reasonable to conclude that the reasons for which the property was transferred or loaned to the recipient did not include the relationship between the transferor and

(i) any person or partnership that was

(A) beneficially interested in the trust,

(B) a trustee of the trust,

(C) a person having influence over the operation of the trust or the enforcement of its terms, or

(D) a person having influence over the selection or appointment of any person or partnership referred to in any of clauses (A) to (C) or this clause, or

(ii) any group at least one of the members of which is described in subparagraph (i).

"connected contributor" « contribuant rattaché »

"connected contributor" to a trust at any time means a person (including any person who has ceased to exist) who is a contributor to the trust at that time, other than

(*a*) an individual (other than a trust) who was, at or before that time, resident in Canada for a period of, or periods the total of which is, not more than 60 months, and

(*b*) a person who would not be a contributor to the trust at that time if

(i) the transfers and loans referred to in paragraph (*a*) of the definition "contribution" made by the person at a non-resident time of the person were not taken into account,

(ii) the particular transfers and loans referred to in paragraph (*b*) of that definition made by the person at a non-resident time of the person were not taken into account, and

(iii) each obligation referred to in paragraph (*c*) of that definition arising at a non-resident time of the person were not taken into account,

and, for the purpose of this definition, a "non-resident time" of a person means a particular time at which the person is non-resident, where the person was non-resident or not in existence throughout the period that began 60 months before the particular time (or, where the particular time is before **[ANNOUNCEMENT DATE + 1]** or the trust arose on and as a consequence of the death of the person, 18 months before the particular time) and ends 60 months after the particular time.

"contribution"
« apport »

"contribution" at any time to a trust by a particular person or partnership means

(*a*) a transfer or loan at that time of property to the trust by the particular person or partnership (other than an arm's length transfer);

(*b*) where a particular transfer or loan of property is made by the particular person or partnership (other than an arm's length transfer by the particular person or partnership in respect of the trust) as part of a series of transactions or events that includes another transfer or loan of a property that is made at that time to the trust by another person or partnership, that other transfer or loan to the extent that it can reasonably be considered to have been enabled by the particular transfer or loan; and

(*c*) where the particular person or partnership becomes obligated to make a particular transfer or loan (other than an arm's length transfer by the particular person or partnership in respect of the trust) as part of a series of transactions or events that includes a transfer or loan of a property that is made at that time by another person or partnership, that transfer or loan to the extent that it can reasonably be considered to have been enabled by that obligation.

"contributor"
« contribuant »

"contributor" to a trust at any time means a person or partnership that, at or before that time, has made a contribution to the trust.

"exempt foreign trust"
« fiducie étrangère exempte »

"exempt foreign trust" at a particular time means

(*a*) a non-resident trust, where

(i) each beneficiary of the trust at the particular time is

(A) an individual who, at the time that the trust was created, was, because mental or physical infirmity, dependent on an individual who is a contributor to the trust or on an individual related to such a contributor (which beneficiary is in this paragraph referred to as an "infirm beneficiary"), or

(B) a person who is entitled, only after the particular time, to receive or otherwise obtain the use of any of the trust's income or capital,

(ii) at least one infirm beneficiary suffers at the particular time from a mental or physical infirmity that causes the beneficiary to be dependent on any person,

(iii) each infirm beneficiary is non-resident at any time in the trust's taxation year that includes the particular time (in this definition referred to as the trust's "current year"), and

(iv) each contribution to the trust made at or before the particular time can reasonably be considered to have been, at the time that the contribution was made, made to provide for the maintenance of an infirm beneficiary during the expected period of the beneficiary's infirmity;

(*b*) a non-resident trust, where

(i) the trust was created after the breakdown of a marriage or common-law partnership of two individuals to provide for the maintenance of a beneficiary under the trust who is a child of one of those individuals (which beneficiary is in this paragraph referred to as a "child beneficiary"),

(ii) each beneficiary of the trust at the particular time is

(A) a child beneficiary under 21 years of age at the particular time,

(B) a child beneficiary under 31 years of age at the particular time who is enroled at any time in the trust's current year at an educational institution that is described in clause (v)(A) or (B), or

(C) a person who is entitled, only after the particular time, to receive or otherwise obtain the use of any of the trust's income or capital,

(iii) each child beneficiary is non-resident at any time in the trust's current year,

(iv) each contributor to the trust at the particular time was one of those individuals or a person related to one of those individuals, and

(v) each contribution to the trust, at the time that the contribution was made, was made to provide for the maintenance of a child beneficiary, while the child was either under 21 years of age, or was under 31 years of age and enroled at an educational institution located outside Canada that is

(A) a university, college or other educational institution that provides courses at a post-secondary school level, or

(B) an educational institution that provides courses that furnish a person with skills for, or improve a person's skills in, an occupation;

(*c*) a non-resident trust where

(i) at the particular time, the trust is an agency of the United Nations,

(ii) at the particular time, the trust owns and administers a university described in paragraph (*f*) of the definition "total charitable gifts" in subsection 118.1(1), or

(iii) at any time in the calendar year that includes the particular time or at any time in the preceding calendar year, Her Majesty in right of Canada has made a gift to the trust;

(*d*) a non-resident trust that has a taxation year that ends at or before the particular time where

(i) the trust was created exclusively for charitable purposes and has been operated, throughout the period that began at the time it was created and ends at the particular time, exclusively for charitable purposes,

(ii) where the particular time is more than 24 months after the day on which the trust was created, there is a group of at least 20 persons (other than trusts) at the particular time who are all contributors to the trust and who all deal with each other at arm's length,

(iii) the accounting profit of the trust for each such taxation year would, if the profit were not distributed and the laws described in subparagraph (iv) did not apply, be subject to an income or profits tax in a particular country other than Canada, and

(iv) for each such taxation year, the laws of the particular country exempted the trust from the payment of any income or profits tax to the government of that country in recognition of the charitable purposes for which the trust is operated;

(*e*) a non-resident trust that is, or but for any of paragraphs (*a*) to (*n*) of the definition "retirement compensation arrangement" in subsection 248(1) would be, governed by a retirement compensation arrangement;

(*f*) a non-resident trust that is governed by a foreign retirement arrangement;

(*g*) a non-resident trust that is governed by an employees profit sharing plan;

(*h*) a non-resident trust that is a trust described in paragraph (*c*) of the definition "exempt trust" in subsection 233.2(1); or

(*i*) a prescribed trust.

"resident beneficiary" « bénéficiaire résidant »

"resident beneficiary" at any time under a trust means a person resident in Canada where, at that time,

(*a*) there is a connected contributor to the trust; and

(*b*) the person is a beneficiary under the trust whose interest as a beneficiary under the trust is not solely contingent on the subsequent death of an individual who

(i) is related at that time to a contributor to the trust, or

(ii) would have been related at that time to a contributor to the trust if every individual who existed before that time had existed at that time.

"resident contributor" « contribuant résidant »

"resident contributor" to a trust at any time means a person who is, at that time, both resident in Canada and a contributor to the trust, but does not include an individual (other than a trust) who has not, at that time, been resident in Canada for a period of, or periods the total of which is, more than 60 months.

Rules of application

(2) For the purposes of this section,

(*a*) property is deemed to be transferred by a person or partnership at any time to a trust where, because of a transfer or loan (other than an arm's length transfer) at that time of property to another person or partnership,

(i) the fair market value of one or more properties held at that time by the trust increases, or

(ii) a liability or potential liability of the trust decreases;

(*b*) property is deemed to be transferred by a particular person or partnership at any time to a trust where

(i) at that time, the trust holds property the fair market value of which is derived in whole or in part, directly or indirectly, from properties held by another person or partnership (in this paragraph referred to as the "recipient"),

(ii) property is transferred or loaned at that time by the particular person or partnership (in subparagraph (iii) referred to as the "transferor") to the recipient, and

(iii) it is reasonable to conclude that one of the reasons for which the property was transferred or loaned to the recipient included the relationship between the transferor and

(A) any person or partnership that was

(I) beneficially interested in the trust,

(II) a trustee of the trust,

(III) a person having influence over the operation of the trust or the enforcement of its terms, or

(IV) a person having influence over the selection or appointment of any person or partnership referred to in any of subclauses (I) to (III) or this subclause, or

(B) any group at least one of the members of which is described in clause (A);

(*c*) the fair market value, at the time of the transfer, of property deemed by paragraph (*a*) or (*b*) to have been transferred to the trust is deemed to be the total of all amounts each of which is an amount by which

(i) the fair market value of a property of the trust increased at that time because of the other transfer or loan referred to in paragraph (*a*) or (*b*), or

(ii) a liability or potential liability of the trust decreased at that time because of the transfer or loan referred to in paragraph (*a*) or (*b*);

(*d*) where a property is acquired at any time by a person or partnership as a consequence of the death of an individual, the individual is deemed to have transferred, at that time, the property to the person or partnership;

(*e*) where, at any time, a person or partnership has given a guarantee on behalf of, or has provided any other financial assistance to, another person or partnership, the person or partnership is deemed to have transferred, at that time, property to that other person or partnership;

(*f*) where, at any time after **ANNOUNCEMENT DATE**, a person or partnership renders (otherwise than in the person's capacity as an employee or in the person's or partnership's capacity as agent) any service to, for or on behalf of, another person or partnership (other than any service rendered to a trust that is related to the administration of the trust), the person or partnership is deemed to have transferred, at that time, property to that other person or partnership;

(*g*) where, at any time after **ANNOUNCEMENT DATE**, a particular person or partnership acquires

(i) a share of the capital stock of a corporation from the corporation,

(ii) a beneficial interest in a trust (otherwise than as a consequence of a disposition of the interest by a beneficiary under the trust),

(iii) an interest in a partnership (otherwise than as a consequence of a disposition of the interest by a member of the partnership), or

(iv) indebtedness owing by a corporation, trust or partnership from the corporation, trust or partnership, the corporation, trust or partnership referred to in subparagraph (i), (ii), (iii) or (iv), as the case may be, is deemed to have transferred, at that time, the share, interest or debt to the particular person or partnership;

(*h*) where, at any time after **ANNOUNCEMENT DATE**, a particular person or partnership grants to another person or partnership a right to acquire or to be loaned property, the particular person or partnership is deemed to have transferred property at that time to that other person or partnership;

(*i*) the fair market value of property deemed by paragraph (*e*), (*f*) or (*h*) to have been transferred is the fair market value, at the time of the transfer, of the assistance, service or right to which the property relates;

(*j*) for greater certainty, where at any time a particular person or partnership becomes obligated to do an act that would constitute the transfer of a property to another person or partnership if the act occurred, the particular person or partnership is deemed to have become obligated at that time to transfer property to that other person or partnership;

(*k*) where, at a particular time, a particular trust makes a contribution to another trust, the contribution is deemed to have been made jointly by the particular trust and by each person or partnership that, at the particular time, is a contributor to the particular trust;

(*l*) where a particular trust makes a contribution to another trust, the contribution is made at the direction, or with the concurrence, of another person and it is reasonable to conclude that one of the reasons the contribution is made to the other trust is to enable that other person to avoid liability under paragraph (3)(*d*) in respect of the other trust, the contribution is deemed to be made jointly by the particular trust and by that other person;

(*m*) where, at a particular time, a particular partnership makes a contribution to a trust, the contribution is deemed to have been made jointly by the particular partnership and by each person or partnership that, at the particular time, is a member of the particular partnership (other than a member of the particular partnership where, by operation of any law governing the partnership arrangement, the liability of the member as a member of the particular partnership is limited);

(*n*) where a partnership makes a contribution to a trust, the contribution is made at the direction, or with the concurrence, of another person and it is reasonable to conclude that one of the reasons the contribution is made to the trust is to enable that other person to avoid liability under paragraph (3)(*d*) in respect of the trust, the contribution is deemed to be made jointly by the partnership and by that other person;

(*o*) where a corporation makes a contribution to a trust, the contribution is made at the direction, or with the concurrence, of another person, and it is reasonable to conclude that one of the reasons the contribution is made to the trust is to enable that other person to avoid liability under paragraph (3)(*d*) in respect of the trust, the contribution is deemed to be made jointly by the corporation and by that other person; and

(*p*) subject to subsection (9), the fair market value of a contribution to a trust at the time it was made is deemed to be the fair market value, at the time of the contribution, of the property that was the subject of the contribution.

Liabilities of non-resident trust and others

(3) Where a trust (other than an exempt foreign trust) is non-resident at the end of a taxation year of the trust and, at that time, there is a resident contributor to the trust or a resident beneficiary under the trust,

(*a*) subject to subsection (4), the trust is deemed to be resident in Canada throughout the year for the purposes of

(i) applying section 2 and computing the trust's income for the year,

(ii) applying subsection (5), clause 53(2)(*h*)(i.1)(B), the definition "non-resident entity" in subsection 94.1(1), subsections 104(13.1) to (29) and 107(5), section 115 and sections 233.3 and 233.4,

(iii) determining the liability of the trust for tax under Part XIII on amounts paid or credited to the trust, and

(iv) determining the rights and obligations of the trust under Divisions I and J;

(*b*) for the purposes of section 126

(i) the trust's income for the year (other than the portion of the income that, but for this subsection, would be the trust's taxable income earned in Canada) is deemed to be income of the trust from sources in the country other than Canada in which the trust would, but for this subsection, be resident, and

(ii) such part of any income or profits tax paid by the trust for the year (other than any tax paid because of this section) that can reasonably be regarded as having been paid in respect of the amount determined under subparagraph (i) is deemed to be the non-business-income tax paid by the trust to the government of that country;

(*c*) where the trust was non-resident throughout the preceding taxation year for the purpose of computing its income for that preceding year, for the purpose of subsection 128.1(1) the trust is deemed to have become resident in Canada immediately after the end of that preceding year; and

(*d*) subject to subsection (7),

(i) each person who at any time in the year is a resident contributor to the trust or a resident beneficiary under the trust shall have, jointly and severally with the trust and with each other such person, the rights and obligations of the trust in respect of the year under Divisions I and J and subsection 180.1(4), and

(ii) each such person shall be subject to the provisions of Part XV in respect of those rights and obligations.

Excluded provisions

(4) Paragraph (3)(*a*) does not apply for the purposes of

(*a*) the definition "exempt foreign trust" in subsection (1);

(*b*) computing any income or loss from property, or any taxable capital gain or allowable loss, because of the application of subsection 75(2);

(*c*) paragraph 107.4(1)(*c*) (other than subparagraph 107.4(1)(*c*)(i)), paragraph (*a*) of the definition "mutual fund trust" in subsection 132(6), and subparagraph (*f*)(ii) of the definition "disposition" in subsection 248(1); and

(*d*) determining the liability of a person that arises because of the application of section 215, except as the Minister otherwise permits in writing.

Ceasing to reside in Canada

(5) A trust is deemed to have ceased to be resident in Canada at any time where

(*a*) that time is in a particular period that, but for this subsection and subsection 128.1(4), would be a taxation year of the trust that immediately follows a taxation year of the trust throughout which the trust was resident in Canada because of the application of subsection (3);

(*b*) the trust is non-resident at the end of the particular period;

(*c*) there was a resident contributor to the trust, or a resident beneficiary under the trust, at the beginning of the particular period; and

(*d*) that time is the earliest time in the particular period at which there is neither a resident contributor to the trust nor a resident beneficiary under the trust.

Becoming or ceasing to be an exempt foreign trust

(6) Where at any time a trust becomes or ceases to be an exempt foreign trust (otherwise than because of becoming resident in Canada),

(*a*) the trust's taxation year that would otherwise include that time is deemed to have ended immediately before that time and a new taxation year of the trust is deemed to have begun at that time; and

(*b*) for the purpose of determining the trust's fiscal period after that time, the trust is deemed not to have established a fiscal period before that time.

Limit to amount recoverable

(7) Notwithstanding subsection (3), the amount recoverable under paragraph (3)(*d*) at any time from a person in respect of a trust and a particular taxation year of the trust shall not exceed the recovery limit at that time of the person in respect of the trust and the particular year where

(*a*) except where subparagraph (*b*)(ii) would apply if the portion of that subparagraph after clause (*b*)(ii)(B) were read as "is not more than $10,000", the person has filed on a timely basis under section 233.2 all information returns required to be filed by the person before that time in respect of the trust (or within such later period as is acceptable to the Minister);

(*b*) either

(i) the person is liable under paragraph (3)(*d*) in respect of the trust and the particular year solely because the person was a resident beneficiary under the trust at the end of the particular year, or

(ii) at the end of the particular year, the total of all amounts each of which is the fair market value, at the time it was made, of a contribution to the trust before the end of the particular year by

(A) the person, or

(B) another person not dealing at arm's length with the person,

is not more than the greater of $10,000 and 10% of the total of all amounts each of which was the fair market value, at the time it was made, of a contribution to the trust before the end of the particular year; and

(*c*) it is reasonable to conclude that each transaction or event that occurred before the end of the particular year at the direction of, or with the concurrence of, the person satisfied the following conditions:

(i) none of the purposes of the transaction or event was to enable the person to minimize liability under paragraph (3)(*d*) in respect of the trust, and

(ii) the transaction or event was not part of a series of transactions or events any of the purposes of which was to enable the person to minimize liability under paragraph (3)(*d*) in respect of the trust.

Recovery limit

(8) For the purpose of subsection (7), the recovery limit at a particular time of a person in respect of a trust and a particular taxation year of the trust is the amount, if any, by which the greater of

(*a*) the total of all amounts each of which is

(i) an amount paid before the particular time to the person by the trust because of the interest of the person as a beneficiary under the trust,

(ii) an amount the payment of which by the trust the person is at the particular time entitled to enforce because of the interest of the person as a beneficiary under the trust,

(iii) an amount (other than an amount described in subparagraph (i)) received before the particular time by the person on the disposition of an interest as a beneficiary under the trust, or

(iv) the fair market value of a benefit received or enjoyed by the person from or under the trust (other than a benefit described in any of subparagraphs (i) to (iii)), and

(*b*) the total of all amounts each of which is the fair market value, at the time it was made, of a contribution to the trust before the particular time by the person,

exceeds

(*c*) the total of all amounts each of which is an amount recovered before the particular time from the person in connection with a liability of the person arising under subsection (3) in respect of the trust and the particular year or a preceding taxation year of the trust.

Determination of fair market value-special case

(9) For the purposes of applying subparagraph (7)(*b*)(ii) and determining the recovery limit under subsection (8), where a contribution is made at any time by a person or partnership to a trust as a consequence of a transaction that is, or as a consequence of a series of transactions or events that includes, the transfer at that time to the trust of a particular property that is a share, a right to acquire a share, or other property primarily deriving its value from a share or a right to acquire a share, the fair market value of the contribution at the time it is made is deemed to be the greater of

(*a*) the fair market value of the contribution at that time, determined without reference to this subsection, and

(*b*) the fair market value of the particular property, or property substituted for the particular property, at the end of the third calendar year that ends after that time.

(2) Subsection (1) applies to taxation years of trusts that begin after 2000, except that the definition "contribution" in subsection 94(1) of the Act, as enacted by subsection (1), shall not apply to

(*a*) a payment made to a trust before 2002 in satisfaction of any amount payable to the trust; or

(*b*) a repayment made before 2005, in accordance with terms of repayment established before [ANNOUNCEMENT DATE + 1], to a trust of a loan made by the trust.

11. (1) Section 94.1 of the Act is replaced by the following:

Foreign Investment Entities – Accrual Treatment

Definitions

94.1(1) The definitions in this subsection apply in this section and sections 94.2 and 94.3.

"carrying value"
« valeur comptable »

"carrying value" at any time of property of an entity means

(*a*) where a balance sheet of the entity is prepared as of that time in accordance with accounting principles substantially similar to generally accepted accounting principles used in Canada, the balance sheet is distributed not later than three months after that time to holders of participating interests in the entity at that time and the property is valued in the balance sheet, the amount at which the property is valued in the balance sheet; and

(*b*) in any other case, the amount at which the property would be valued for the purpose of the entity's balance sheet as of that time if a balance sheet of the entity were prepared in accordance with generally accepted accounting principles used in Canada at that time.

"entity"
« entité »

"entity" includes a trust, a corporation, an organization and a fund, but does not include a partnership unless a contrary intent is evident.

"excluded investment business"
« entreprise de placement exclue »

"excluded investment business" of a corporation in a period means an investment business of the corporation in the period where, throughout the part of the period during which the business was carried on, all or substantially all of the corporation's assets used or held in the business are participating interests or debt issued by one or more other corporations

(*a*) each of which is related to the corporation or is a corporation in which the corporation has a significant interest; and

(*b*) the principal business carried on by each of which in the period is not an investment business.

"exempt interest"
« participation
exempte »

"exempt interest" of a taxpayer in a foreign investment entity at any time means

(*a*) a participating interest held by the taxpayer at that time in a controlled foreign affiliate of the taxpayer;

(*b*) property held by the taxpayer at that time that is a share of a class of the capital stock of a particular corporation or a right to acquire a share of the class, where

(i) the class is, throughout the part of the taxpayer's taxation year that includes that time (which year is in this definition referred to as the "relevant year") during which shares of the class (or rights to acquire shares of the class) are held by the taxpayer, widely-held, actively traded on a regular basis and listed on a prescribed stock exchange, and

(ii) either

(A) the particular corporation's principal business was not an investment business in the period referred to in subparagraph (i), or

(B) the particular corporation is a qualifying corporation in the period referred to in subparagraph (i);

(*c*) where the taxpayer is a financial institution (within the meaning assigned by subsection 142.2(1)) in the relevant year, a participating interest that is a mark-to-market property (within the meaning assigned by subsection 142.2(1)) for that year; and

(*d*) a participating interest of the taxpayer in a testamentary trust that, before that time, has never been acquired for consideration.

"exempt taxpayer"
« contribuable
exempté »

"exempt taxpayer" for a taxation year means

(*a*) an individual (other than a trust) who, before the end of the year, was resident in Canada for a period of, or periods the total of which is, not more than 60 months, but not including an individual who, before the end of the year, was never non-resident; and

(*b*) an entity the taxable income of which for a period any part of which occurs in the year is exempt from tax under this Part because of subsection 149(1) (otherwise than because of paragraph 149(1)(*q*.1), (*t*) or (*z*)).

"foreign bank"
« banque
étrangère »

"foreign bank" has the same meaning as in subsection 95(1).

"foreign investment
entity"
« entité de
placement
étrangère »

"foreign investment entity" at any time means a non-resident entity at that time except where, at the end of its taxation year that includes that time,

(*a*) the entity would be an exempt foreign trust (within the meaning assigned by subsection 94(1)) if the definition "exempt trust" in subsection 233.2(1) were read without reference to paragraph (*c*) of that definition;

(*b*) the entity is

(i) a personal trust, and

(ii) not a non-discretionary trust; or

(*c*) the carrying value of all of the entity's investment property is not more than one-half of the carrying value of all of the entity's property.

"investment business"
« entreprise de placement »

"investment business" of an entity in a period means a business carried on by the entity at any time in the period the principal purpose of which is to derive income from property (including interest, dividends, rents, royalties or any similar return on investment or any substitute for such a return), income from the insurance or reinsurance of risks, income from the factoring of trade accounts receivable, or profits from the disposition of indebtedness or properties described in any of paragraphs (*a*) to (*d*) or (*f*) to (*l*) of the definition "investment property", unless it is established that, throughout the part of the period during which the business was carried on by the entity, the business (other than any business conducted principally with persons with whom the entity does not deal at arm's length) is

(*a*) a business carried on by the entity as a foreign bank, a trust company, a credit union or an insurance corporation, the activities of which are regulated under the laws of the country in which the business is principally carried on;

(*b*) the development of real estate for sale;

(*c*) the rental of real estate held by the entity if the management, maintenance, and other services in respect of the real estate are provided principally by the employees of the entity or of a corporation related to it; or

(*d*) the development of foreign resource property.

"investment property"
« bien de placement »

"investment property" of an entity includes property that is

(*a*) a share of the capital stock of a corporation;

(*b*) an interest in a partnership;

(*c*) an interest in a trust;

(*d*) an interest in any other entity;

(*e*) indebtedness, other than accounts receivable that arose from the sale of tangible property or services in the ordinary course of a business of the entity that is not an investment business;

(*f*) an annuity;

(*g*) a commodity or commodity future purchased or sold, directly or indirectly in any manner whatever, on a commodities or commodities futures exchange (except a commodity manufactured, produced, grown, extracted or processed by the entity or a person to whom the entity is related, otherwise than because of a right referred to in paragraph 251(5)(*b*), or a commodity future in respect of such a commodity);

(*h*) real estate;

(*i*) a Canadian resource property or foreign resource property;

(*j*) currency;

(*k*) a derivative financial product (other than a commodity future to which the exception in paragraph (*g*) applies); or

(*l*) an interest, option, or right in respect of property included in any of paragraphs (*a*) to (*k*).

"non-resident entity"
« entité non-résidente »

"non-resident entity" at any time means

(*a*) a corporation or trust that is non-resident at that time; and

(*b*) any entity (other than a corporation or trust)

(i) organized under the laws of a jurisdiction outside Canada, or

(ii) the governance of which is provided at that time under the laws of a jurisdiction outside Canada.

"participating interest"
« participation déterminée »

"participating interest" in an entity means (*a*) where the entity is a corporation,

(i) a share of the capital stock of the corporation, and

(ii) a right to acquire a share of the capital stock of the corporation;

(*b*) where the entity is a trust,

(i) a beneficial interest in the trust, and

(ii) a right to acquire a beneficial interest in the trust; and

(*c*) in any other case, an interest in the entity or a right to acquire an interest in the entity.

"qualifying corporation" « société admissible »

"qualifying corporation" in a period means a particular corporation all or substantially all of the assets of which are, throughout the period, any combination of

(*a*) properties (other than investment properties); and

(*b*) shares and debt issued by one or more other corporations each of which

(i) is, at any time in the period, a corporation all of the shares of which (other than directors' qualifying shares) are held by

(A) the particular corporation,

(B) a corporation related to the particular corporation, or

(C) any combination of corporations described in clauses (A) and (B), and

(ii) is either

(A) a corporation the principal business of which throughout the period is

(I) an excluded investment business, or

(II) a business that is not an investment business, or

(B) a qualifying corporation in the period.

"taxation year"
« année d'imposition »

"taxation year" of a non-resident entity means

(*a*) in the case of a corporation the accounts of which have ordinarily been made up for a period not exceeding 53 weeks, that period; and

(*b*) in any other case, a calendar year.

Conditions for application of tax regime for foreign investment entities

(2) This subsection applies to a taxpayer for a particular taxation year in respect of a participating interest held in the particular year by the taxpayer in a non-resident entity where

(*a*) the taxpayer is not an exempt taxpayer for the particular year;

(*b*) a taxation year of the entity ended at or before the end of the particular year;

(*c*) at the end of the latest of the entity's taxation years referred to in paragraph (*b*), the entity was a foreign investment entity;

(*d*) if the interest or identical property to the interest was held by the taxpayer at the end of the latest of the entity's taxation years referred to in paragraph (*b*), none of the interest and each identical property was, at the end of that year, an exempt interest in respect of the taxpayer; and

(*e*) if neither the interest nor identical property to the interest was held by the taxpayer at the end of the latest of the entity's taxation years referred to in paragraph (*b*), none of the interest and each identical property was, at the latest time in the particular year at which the interest or identical property was held by the taxpayer, an exempt interest in respect of the taxpayer.

Income inclusion and deduction

(3) Subject to subsection (4), where, at any time in a particular taxation year of a taxpayer, the taxpayer holds a participating interest,

or two or more identical participating interests, in a non-resident entity and subsection (2) applies to the taxpayer for the particular year in respect of those interests, in computing the taxpayer's income for the particular year in respect of such of those interests that are held by the taxpayer at the end of a taxation year of the entity (in this subsection referred to as the "relevant interests") that ends in the particular year, except where the taxpayer is non-resident at the end of the entity's year,

(*a*) there shall be added the positive amount, if any, determined by the formula

$$A - B - C - D$$

where

A is the taxpayer's income allocation in respect of the relevant interests for the entity's year,

B is the taxpayer's loss allocation in respect of the relevant interests for the entity's year,

C is the specified tax allocation of the taxpayer for the entity's year in respect of the relevant interests, and

D is the amount, if any, by which

(i) the amount determined in respect of the taxpayer under subparagraph (*b*)(i) for the preceding taxation year of the entity in respect of the relevant interests or identical properties

exceeds

(ii) the amount determined for that preceding year in respect of the taxpayer under subparagraph (*b*)(ii) in respect of the relevant interests or identical properties; and

(*b*) there may be deducted the lesser of

(i) the absolute value of the negative amount, if any, determined by the formula in paragraph (*a*) in respect of the relevant interests for the entity's year, and

(ii) the amount, if any, by which

(A) the total of all amounts each of which is an amount added under paragraph (*a*) in computing the taxpayer's income in respect of the relevant interests or identical properties for a preceding taxation year of the entity exceeds

(B) the total of all amounts each of which is an amount deductible under this paragraph in computing the taxpayer's income in respect of the relevant interests or identical properties for a preceding taxation year of the entity.

Exceptions

(4) Subsection (3) applies to a taxpayer for a taxation year in respect of a participating interest held in the year by the taxpayer in a non-resident entity only where

(*a*) the taxpayer so elects in respect of the interest in prescribed form and files the election with the Minister not later than the taxpayer's filing-due date for the year;

(*b*) the taxpayer filed an election under paragraph (*a*) in respect of the interest (or property identical to it) for each preceding taxation year that began after 2000 and in which the interest or the identical property was held by the taxpayer;

(*c*) subsection (17) does not apply to the taxpayer for the year in respect of the interest;

(*d*) subsection 94.2(3) does not, because of subsection 94.2(9), apply to the taxpayer for the year or a preceding taxation year in respect of the interest or identical property to the interest;

(*e*) the taxpayer is not a foreign investment entity;

(*f*) the interest is not a right to acquire

(i) shares of the capital stock of the entity, or

(ii) an interest in the entity; and

(*g*) the interest would, if this Act were read without reference to subparagraph 39(1)(*a*)(ii.3) and section 94.2, be capital property.

Income allocation

(5) For the purpose of subsection (3), the income allocation of a particular taxpayer in respect of a participating interest, or two or more identical participating interests, of the particular taxpayer in a foreign

investment entity for a particular taxation year of the entity is the amount determined by the formula

$$A \times \frac{B}{C}$$

where

A is the amount that would be the income of the entity for the particular year if

(*a*) except for the purposes of section 91, paragraph (4)(*e*), subsection 107.4(1) and paragraph (*f*) of the definition "disposition" in subsection 248(1), the entity had been a taxpayer resident in Canada throughout the entity's existence,

(*b*) each property held by the entity at the beginning of the entity's fresh start year in respect of the particular taxpayer had been

(i) disposed of by the entity immediately before that time for proceeds equal to its fair market value at that time, and

(ii) reacquired by the entity at that time at a cost equal to that fair market value,

(*c*) for the entity's fresh start year in respect of the particular taxpayer and for each following taxation year of the entity, each deduction in computing the entity's income that is contingent on a claim by the entity had been claimed by the entity to the extent, and only to the extent, designated by the particular taxpayer in prescribed form filed with the Minister with the particular taxpayer's return of income for the particular taxpayer's taxation year in which that fresh start year or the following year, as the case may be, ends,

(*d*) the entity had deducted the greatest amounts that it could have claimed or deducted as a reserve under sections 20, 138 and 140 for its taxation year that precedes its fresh start year in respect of the particular taxpayer,

(*e*) for the purposes of applying sections 37, 65 to 66.4 and 66.7, the entity had not existed before the entity's fresh start year in respect of the particular taxpayer,

(*f*) this Act were read without reference to subsections 20(11) and (12) and 104(4) to (6),

(*g*) where the particular taxpayer is a corporation resident in Canada, dividends received by the entity in the particular year from a foreign affiliate of the particular taxpayer were included in computing the income of the entity for the particular year only where

(i) the particular taxpayer did not have a qualifying interest (within the meaning assigned by paragraph 95(2)(*m*)) in the affiliate at the time the dividends were received, or

(ii) taking into account the application of paragraphs (*a*) and (*i*), subsection 94.2(4) applied for the purpose of computing the entity's income for the particular year in respect of the entity's participating interest in the affiliate,

(*h*) where the entity holds at any time in the particular year a participating interest in a non-resident entity, the description of D in paragraph 94.2(4)(*a*) did not apply in respect of that interest, and

(*i*) the words "controlled foreign affiliate of the taxpayer" in paragraph (*a*) of the definition "exempt interest" referred to a controlled foreign affiliate of the particular taxpayer and not to a controlled foreign affiliate of the entity;

B is the fair market value of those interests at the end of the particular year; and

C is the fair market value of all participating interests in the entity (other than rights to acquire shares of the capital stock of, or interests in, the entity) at the end of the year.

Fresh start year

(6) For the purpose of subsection (5), the fresh start year of a foreign investment entity in respect of a taxpayer is the first taxation year of the entity

(*a*) that ends in a taxation year of the taxpayer that begins after 2000; and

(*b*) any time in which the taxpayer holds a participating interest in the entity.

Loss allocation

(7) For the purpose of subsection (3), the loss allocation of a taxpayer in respect of a participating interest, or two or more identical participating interests, of the taxpayer in a foreign investment entity for a taxation year of the entity is the amount that would, if paragraphs (*a*)

to (*i*) of the description of A in subsection (4) applied, be determined by the formula

$$(A - B) \times \frac{C}{D}$$

where

A is the total of all amounts each of which is a loss of the entity for the year from business or property;

B is the amount determined under paragraph 3(*c*) in respect of the entity for the year;

C is the fair market value of those interests at the end of the year; and

D is the fair market value of all participating interests in the entity (other than rights to acquire shares of the capital stock of, or interests in, the entity) at the end of the year.

Specified tax allocation

(8) For the purpose of subsection (3), the specified tax allocation of a taxpayer for a particular taxation year of a non-resident entity in respect of a participating interest, or two or more identical participating interests, held by the taxpayer at the end of the particular year is the total of all amounts each of which is the amount determined, in respect of a taxation year of the entity (in this subsection referred to as the "liability year") that is the particular year or a preceding taxation year, by the formula

$$A \times (B/C) \times D$$

where

A is

(*a*) where the liability year ends in a taxation year of the taxpayer that begins after 2000, the income or profits tax paid in the particular year by the particular entity for the liability year, and

(*b*) in any other case, nil;

B is

(*a*) where the taxpayer did not hold those interests or identical properties at the end of the liability year, nil, and (*b*) in any other case, the total fair market value of those interests and identical properties that are held by the taxpayer at the end of the liability year;

C is the fair market value of all participating interests in the entity (other than rights to acquire shares of the capital stock of, or interests in, the entity) at the end of the liability year; and

D is the taxpayer's relevant tax factor (within the meaning assigned by subsection 95(1)) for the particular year.

Adjusted cost base

(9) In computing the adjusted cost base to a taxpayer of a participating interest in an entity at and after the end of a taxation year of the entity,

(*a*) there shall be added the amount, if any, added under subsection (3) in computing the taxpayer's income in respect of the interest for the entity's year (or that would have been so added if this Act were read without reference to subsection 56(4.1) and sections 74.1 to 75); and

(*b*) there shall be deducted the amount, if any, deducted under subsection (3) in computing the taxpayer's income in respect of the interest for the entity's year (or that would have been so deducted if this Act were read without reference to subsection 56(4.1) and sections 74.1 to 75).

Property deemed owned by an entity

(10) Where at any time a particular entity has a significant interest in a corporation, a partnership or a non-discretionary trust, for the purposes of this section and section 94.2,

(*a*) the carrying value at that time of each participating interest held at that time by the particular entity in the corporation, partnership or trust (and of each debt owing to the particular entity by the corporation, partnership or trust that is investment property of the particular entity) is deemed to be nil;

(*b*) the property owned at that time by the corporation is deemed to be owned at that time by the particular entity and to have a carrying value at that time equal to the amount determined by the formula

$$A \times B/C$$

where

A is the carrying value of the property to the corporation at that time,

B is the total of

(i) the fair market value at that time of the shares of the corporation owned at that time by the particular entity, and

(ii) the fair market value at that time of debts (other than debts that are not investment properties) owing at that time to the particular entity by the corporation, and

C is the total of

(i) the fair market value at that time of all the issued shares of the corporation outstanding at that time, and

(ii) the fair market value at that time of debts owing at that time by the corporation (other than debts that are not investment properties);

(*c*) the property owned at that time by the partnership is deemed to be owned at that time by the particular entity and to have a carrying value at that time equal to the amount determined by the formula

$$D \times E/F$$

where

D is the carrying value of the property to the partnership at that time,

E is the total of

(i) the fair market value of the interests in the partnership owned at that time by the particular entity, and

(ii) the fair market value of debts (other than debts that are not investment properties) owing at that time to the particular entity by the partnership, and

F is the total of

(i) the fair market value at that time of all interests in the partnership, and

(ii) the fair market value at that time of debts owing by the partnership (other than debts that are not investment property); and

(*d*) the property owned at that time by the trust is deemed to be owned at that time by the particular entity and to have a carrying value at that time equal to the amount determined by the formula

$$G \times H/I$$

where

G is the carrying value of the property to the trust at that time,

H is the total of

(i) the fair market value of the interests in the trust owned at that time by the particular entity, and

(ii) the fair market value of debts (other than debts that are not investment properties) owing at that time to the particular entity by the trust, and

I is the total of

(i) the fair market value at that time of all interests in the trust, and

(ii) the fair market value at that time of debts owing by the trust (other than debts that are not investment properties).

Significant interest in an entity

(11) For the purposes of subsection (10) and section 94.2, an entity has a significant interest in

(*a*) a corporation at any time if at that time the entity holds shares of the capital stock of the corporation

(i) that would give the entity 25% or more of the votes that could be cast under all circumstances at an annual meeting of shareholders of the corporation, and

(ii) having a fair market value of 25% or more of the fair market value of all of the issued and outstanding shares of the corporation;

(*b*) a partnership at any time if at that time the entity holds an interest in the partnership having a fair market value of 25% or more of the fair market value of all interests in the partnership; and

(*c*) a non-discretionary trust at any time if at that time the entity holds interests in the trust having a fair market value of 25% or more of the fair market value of all interests in the trust.

Entity treated as controlled foreign affiliate

(12) Where

(*a*) at a particular time in a particular taxation year of a taxpayer, the taxpayer, or a particular controlled foreign affiliate of the taxpayer, holds a participating interest in a non-resident entity,

(*b*) a taxation year of the entity ends at or before the end of the particular year,

(*c*) the principal business of the entity in the particular year is an excluded investment business or a business that is not an investment business,

(*d*) the entity is, at the end of the particular year, a foreign affiliate of the taxpayer in respect of which the taxpayer has a qualifying interest (as defined in paragraph 95(2)(*m*)),

(*e*) the taxpayer elects in prescribed form in the taxpayer's return of income for the particular year, and

(*f*) the taxpayer has not elected under this subsection in respect of the entity for any taxation year of the taxpayer that precedes the particular year,

subject to subsection (17), the entity is deemed to be a controlled foreign affiliate of the taxpayer throughout the period

(*g*) that begins at the earliest time in the particular year at which the entity is a foreign affiliate of the taxpayer, and

(*h*) that ends at the earlier of

(i) the earliest subsequent time at which the entity is not a foreign affiliate of the taxpayer, and

(ii) the end of the first subsequent taxation year of the taxpayer in which the principal business of the entity is an investment business (other than an excluded investment business).

Exception for qualifying dispositions and issues

(13) For the purpose of determining whether an entity is a foreign investment entity at the end of a taxation year of the entity in which a qualifying disposition of that or another entity, or a qualifying issue of that or another entity, occurred, each investment property received by either entity as consideration for the qualifying disposition or the qualifying issue, and investment property substituted therefor, is deemed to have a carrying value of nil.

Qualifying disposition

(14) For the purpose of subsection (13), a qualifying disposition of an entity is a transaction or part of a series of transactions or events as a consequence of which the entity disposes, to a person with whom the entity deals at arm's length, of all or substantially all of the assets used or held for the purpose of gaining or producing income from a business (other than an investment business) carried on by it.

Qualifying issue

(15) For the purpose of subsection (13), a qualifying issue of an entity is an issue by the entity of a debt of, or a participating interest in, the entity to a person or partnership, otherwise than as part of a series of transactions or events that includes the disposition of a debt of, or a participating interest in, the entity (or another entity with which the entity does not deal at arm's length) by

(*a*) the person or partnership (or another person or partnership with which the person or partnership does not deal at arm's length);

(*b*) a trust in which the person or partnership (or another person or partnership with which the person or partnership does not deal at arm's length) is beneficially interested; or (*c*) a partnership in which the person or partnership (or another person or partnership with which the person or partnership does not deal at arm's length) has a direct or indirect interest.

Demand for information

(16) Subsection (17) applies to a taxpayer for a taxation year of the taxpayer where

(*a*) the Minister demands, in writing, from the taxpayer additional information for the purpose of enabling the Minister to make a determination of an amount that, but for subsection (17), would be required to be added or deducted (otherwise than under subsection 104(13)) in computing the income of the taxpayer for the year

(i) because of the application of section 91 and an election under subsection (12), or

(ii) because of the application of subsection (3) to a participating interest in an entity; and

(*b*) sufficient information to make the determination is not delivered to the Minister within 60 days (or within such longer period as is acceptable to the Minister) after the Minister sends the demand.

Effect of insufficient information

(17) Where this subsection applies to a taxpayer for a taxation year because of subsection (16), for the purpose of computing the taxpayer's income for the year and following taxation years,

(*a*) where paragraph (16)(*a*) applies because of subparagraph (16)(*a*)(*i*),

(i) the election referred to in that subparagraph is deemed not to have been made, and

(ii) subsection (3) shall not apply in respect of the foreign affiliate that was the subject of the election; and

(*b*) where paragraph (16)(*a*) applies because of subparagraph (16)(*a*)(ii), subsection (3) shall not apply in respect of the entity referred to in that subparagraph.

Foreign Investment Entities – Mark-to-market

Definitions

94.2 (1) In this section,

(*a*) the definitions in subsection 94.1(1) apply;

(*b*) subject to subsections (6) and (13) to (17), "deferral amount" of a taxpayer in respect of a participating interest in an entity means the positive or negative amount determined by the formula

$$A \times (B - C)$$

where

A is

(i) if on **ANNOUNCEMENT DATE** the interest was capital property held by the taxpayer, 2/3, and

(ii) in any other case, 1,

B is

(i) the fair market value of the interest at the first time in a particular taxation year of the taxpayer at which the taxpayer was resident in Canada where

(A) the taxpayer held the interest at the end of the preceding taxation year,

(B) at the end of that preceding year, the taxpayer was resident in Canada or the interest was taxable Canadian property,

(C) subsection (4) did not apply to the taxpayer for the purpose of computing the taxpayer's income in respect of the interest for any preceding taxation year, and

(D) subsection (4) applies to the taxpayer for the purpose of computing the taxpayer's income in respect of the interest for the particular year, and

(ii) nil in any other case, and

C is

(i) if subparagraph (i) of the description of B applies in respect of the interest, the cost amount of the property immediately before the first time in the particular year at which the taxpayer was resident in Canada, and

(ii) nil in any other case; and

(*c*) "gross-up factor" for a deferral amount is

(i) if the amount determined for A in respect of the deferral amount is 2/3, 3/2, and

(ii) in any other case, 1.

Rules of application

(2) For the purposes of this section

(*a*) identical participating interests held by a taxpayer are deemed to be disposed of in the order in which they were acquired by the taxpayer, determined without reference to any other provision of this Act; and

(*b*) subsections 94.1(10) and (11) apply.

Where mark-to-market method applies

(3) Subject to paragraph (5)(*b*), this subsection applies to a taxpayer throughout a taxation year in respect of a participating interest held in the year by the taxpayer in a non-resident entity where

(*a*) subsection (9) or (10) applies to the taxpayer for the year in respect of the interest; or

(*b*) both

(i) subsection 94.1(2) applies to the taxpayer for the year in respect of the interest, and

(ii) because of subsection 94.1(4), subsection 94.1(3) does not apply to the taxpayer for the year in respect of the interest.

Mark-to-market

(4) Where subsection (3) applies to a taxpayer throughout a taxation year in respect of a participating interest in a non-resident entity, in computing the taxpayer's income for the year in respect of the interest

(*a*) there shall be added the positive amount, if any, determined by the formula

$$(A + B + C + D) - (E + F + G)$$

where

A is the total of all amounts each of which is the taxpayer's proceeds from a disposition of the interest in the year (other than a disposition deemed to arise because of subsection 128.1(4) or 149(10)),

B is

(i) if the taxpayer held the interest at the end of the year, the fair market value of the interest at that time (determined before taking into account any amount payable at the end of the year from the entity in respect of the interest), and

(ii) in any other case, nil,

C is the total of all amounts (other than an amount to which the description of A applies) received by the taxpayer in the year from the entity in respect of the interest,

D is

(i) the taxpayer's deferral amount in respect of the interest, if

(A) the deferral amount is a positive amount,

(B) the interest was not disposed of by the taxpayer in the year, and

(C) the taxpayer elects in respect of the interest in prescribed form filed with the Minister not later than the taxpayer's filing-due date for the year,

(ii) the taxpayer's deferral amount in respect of the interest if

(A) the taxpayer disposed of the interest in the year, and

(B) no election was made under subparagraph (i) in respect of the interest by the taxpayer for a preceding taxation year, and

(iii) in any other case, nil,

E is the total of all amounts each of which is the cost at which the taxpayer acquired the interest in the year (otherwise than because of an acquisition deemed to arise because of subsection 128.1(4) or 149(10)),

F is

(i) if the taxpayer held the interest at the beginning of the year, the fair market value of the interest at that time (determined before taking into account any amount payable at that time from the entity in respect of the interest), and

(ii) in any other case, nil, and

G is

(i) if the interest was deemed by paragraph (10)(*a*) to be a participating interest in an entity for the preceding taxation year of the taxpayer, the amount that would be deductible under paragraph (*b*) in computing the taxpayer's income for that preceding year in respect of the interest if this subsection were read without reference to subparagraph (*b*)(i), and

(ii) in any other case, nil; and

(*b*) there may be deducted

(i) if the interest was deemed by paragraph (10)(*a*) to be a participating interest in an entity for the year, nil, and

(ii) in any other case, the absolute value of the negative amount, if any, determined by the formula in paragraph (*a*).

Non-resident periods excluded

(5) Where a taxpayer is non-resident at any time in a taxation year

(*a*) for the purpose of subsection (4) (other than the description of D in paragraph (4)(*a*)), the year is deemed to be the period, if any, that begins at the first time in the year at which the taxpayer is resident in Canada and ends at the last time in the year at which the taxpayer is resident in Canada;

(*b*) except for the purposes of subsection (4) and paragraph (*c*), subsection (3) does not apply to the taxpayer at that time; and

(*c*) if the taxpayer is an individual who was non-resident throughout a particular period that is within the period described in paragraph (*a*), at any time in the particular period, the individual holds a participating interest in a non-resident entity and subsection (3) applies to the individual throughout the particular period in respect of the interest,

(i) for the purposes of section 114, the income or loss of the individual in respect of the interest for the particular period shall be determined without reference to this section, and

(ii) in computing the amount determined under paragraph 114(*a*) in respect of the individual for the year

(A) there shall be deducted any amount that would be included under paragraph (4)(*a*) in computing the individual's income in respect of the interest for the particular period if

(I) the value of D in paragraph (4)(*a*) were nil, and

(II) the particular period were a taxation year, and

(B) there shall be added any amount that would be deductible under paragraph (4)(*b*) in computing the individual's income in respect of the interest for the particular period if

(I) the value of D in paragraph (4)(*a*) were nil, and

(II) the particular period were a taxation year.

Foreign partnership – member becoming resident

(6) Where, at a particular time in a fiscal period of a partnership, a person resident in Canada becomes a member of the partnership, or a person who is a member of the partnership becomes resident in Canada and immediately before the particular time no member of the partnership is resident in Canada,

(*a*) all amounts determined under this section shall be determined as if that period began at the first time in that period at which a member of the partnership was resident in Canada;

(*b*) for the purpose of the definition "deferral amount" in paragraph (1)(*b*), as it applies in respect of dispositions that occur after the particular time and before the first subsequent time to which this subsection applies in respect of the partnership, subsection (4) is deemed not to have applied to the partnership for any preceding fiscal period; and

(*c*) where, but for this paragraph, a negative deferral amount would be determined in respect of a participating interest held by the partnership immediately before the particular time, the deferral amount in respect of the interest is deemed to be nil.

Foreign partnership – members ceasing to be resident

(7) Where, at a particular time in a fiscal period of a partnership, a person resident in Canada ceases to be a member of the partnership, or a person who is a member of the partnership ceases to be resident in Canada and immediately after the particular time no member of the partnership is resident in Canada, all amounts determined under this section shall be determined as if that period ended at the last time in that period at which a member of the partnership was resident in Canada.

Application of ss. (6) and (7)

(8) For the purposes of applying subsections (6) and (7) and this subsection,

(*a*) where it can reasonably be considered that one of the main reasons that a member of a partnership is resident in Canada is to avoid the application of subsection (6) or (7), the member is deemed not to be resident in Canada; and

(*b*) where a particular partnership is a member of another partnership at any time,

(i) each person or partnership that is at that time a member of the particular partnership is deemed to be a member of the other partnership at that time,

(ii) each person or partnership that becomes at that time a member of the particular partnership is deemed to become a member of the other partnership at that time, and

(iii) each person or partnership that ceases at that time to be a member of the particular partnership is deemed to cease to be a member of the other partnership at that time.

Tracked interests

(9) Subject to paragraph (5)(*b*), subsection (3) applies to a taxpayer throughout a particular taxation year of the taxpayer in respect of a participating interest in a non-resident entity where

(*a*) the taxpayer holds the interest at any time in the particular year;

(*b*) a taxation year of the entity ends at or before the end of the particular year;

(*c*) the taxpayer is not an exempt taxpayer for the particular year;

(*d*) the entitlement to receive payments from the entity in respect of the interest (or its fair market value) is determined primarily by reference to production, revenue, profit or cash flow from, the fair market value or the use of, or any similar criterion in respect of, a property or group of properties (each of which is referred to in paragraphs (*e*) and (*f*) as a "tracked property");

(*e*) at the end of the latest of the entity's taxation years described in paragraph (*b*), the tracked properties

(i) are not all of the properties that would be owned by the entity if this Act were read without reference to subsection 94.1(10), or

(ii) include properties that would not be owned by the entity if this Act were read without reference to subsection 94.1(10); and

(*f*) either

(i) at the end of the latest of the entity's taxation years described in paragraph (*b*), the total of all amounts each of which is

(A) the carrying value of an investment property that is a tracked property owned at the end of that year by the entity, or

(B) an amount that would, if this Act were read without reference to paragraph 94.1(10)(*a*), be the carrying value of a tracked property that is

(I) owned at the end of the year by the entity,

(II) deemed by paragraph 94.1(10)(*a*) to have a carrying value of nil, and

(III) either a participating interest in a foreign investment entity or indebtedness owing by a foreign investment entity,

exceeds one-half of the total of

(C) all amounts each of which is the entity's carrying value of a tracked property owned by it at the end of that year, and

(D) the carrying value (determined without reference to paragraph 94.1(10)(*a*)) of a tracked property to which subclauses (B)(I) to (III) apply, or

(ii) at the end of the latest of the entity's taxation years described in paragraph (*b*)

(A) the entity, or another non-resident entity, owns an investment property (other than a tracked property owned by the entity), and

(B) it is reasonable to conclude that the production, revenue, profit or cash flow from the investment property, the increase in the fair market value of the investment property, or any other return on the investment property based on a similar criterion, is intended to enable the entity to satisfy all or part of an entitlement referred to in paragraph (*d*).

Treatment of foreign insurance policies

(10) Where, in a particular taxation year of a taxpayer (other than an exempt taxpayer for the particular year), the taxpayer holds a particular interest in an insurance policy that was neither issued in the course of carrying on an insurance business in Canada, the income from which is subject to tax under this Part, nor entered into solely in respect of risks that relate to activities occurring outside Canada or losses in respect of tangible property ordinarily situated outside Canada,

(*a*) subject to paragraph (*b*),

(i) for the purposes of applying subsections (3) and(4) and paragraph (*d*.1) of the definition "specified foreign property" in subsection 233.3(1) to the taxpayer in respect of the particular interest for the particular year,

(A) the particular interest is deemed at each time throughout the particular year that it is held by the taxpayer to be a participating interest in a non-resident entity,

(B) subject to paragraph (5)(*b*), subsection (3) is deemed to apply to the taxpayer throughout the particular year in respect of the particular interest, and

(C) the value of D in paragraph (4)(*a*) is deemed to be nil, and

(ii) section 12.2, paragraphs 56(1)(*d*) and (*j*) and 60(*a*) and (*s*) and sections 138 and 138.1 do not apply in respect of the particular interest for the purpose of computing the taxpayer's income for the year;

(*b*) paragraph (*a*) does not apply to an individual for a taxation year in respect of a policy an interest in which was acquired by the individual more than five years before the individual became resident in Canada unless, after the day that is five years before the day that the individual became resident in Canada, the individual paid premiums in respect of the policy that are in excess of the level that can reasonably be considered to have been contemplated at the time the first interest in the policy was acquired;

(*c*) an interest in an insurance policy is deemed to have been disposed of by a person at the end of a taxation year of the person for proceeds of disposition equal to its fair market value at that time where

(i) paragraph (*a*) did not apply to the person in respect of the interest for the year,

(ii) the person held the interest at the end of the year, and

(iii) paragraph (*a*) applies to the person in respect of the interest for the person's following taxation year;

(*d*) an interest in an insurance policy is deemed to have been acquired by a person at the beginning of a taxation year of the person at a cost equal to its fair market value at that time where

(i) paragraph (*a*) does not apply to the person in respect of the interest for the year,

(ii) the person held the interest at the beginning of the year, and

(iii) paragraph (*a*) applied to the person in respect of the interest for the person's preceding taxation year; and (*e*) for the purposes of this subsection and subsection (4), the fair market value of an interest in an insurance policy, the proceeds of disposition of an interest in an insurance policy and amounts paid to a beneficiary in respect of an interest in an insurance policy shall each be determined without reference to benefits paid, payable or anticipated to be payable, under the policy as a consequence only of a death, sickness, disability or prescribed event.

Change of status of entity

(11) Where a participating interest is held by a taxpayer at the beginning of a taxation year, subsection (4) applied for the purpose of computing the taxpayer's income in respect of the interest for the preceding taxation year and that subsection does not apply for the purpose of computing the taxpayer's income in respect of the interest for the year (otherwise than because the taxpayer became an exempt taxpayer or ceased to reside in Canada),

(*a*) subject to paragraph (*c*), the taxpayer is deemed to have acquired the interest at the beginning of the year at a cost equal to its fair market value at that time;

(*b*) where the interest is capital property at the beginning of the year, in computing the adjusted cost base after that time to the taxpayer of the interest

(i) except where the taxpayer has made an election in respect of the interest under clause (i)(C) of the description of D in paragraph (4)(*a*), there shall be deducted the product of any positive deferral amount in respect of the interest and the gross-up factor for the deferral amount, and

(ii) there shall be added the product of the absolute value of any negative deferral amount in respect of the interest and the gross-up factor for the deferral amount; and

(*c*) where paragraph (*b*) does not apply,

(i) except where the taxpayer has made an election in respect of the interest under clause (i)(C) of the description of D in paragraph (4)(*a*), there shall be deducted in computing the cost to the taxpayer of the interest the lesser of

(A) the product of any positive deferral amount in respect of the interest and the gross-up factor for the deferral amount, and

(B) the cost to the taxpayer of the interest, determined without reference to this subparagraph,

(ii) there shall be included in computing the taxpayer's income for the year in respect of the interest the amount, if any, by which

(A) the amount determined under clause (i)(A) in respect of the interest

exceeds

(B) the amount determined under clause (i)(B) in respect of the interest, and

(iii) there shall be added in computing the cost to the taxpayer of the interest the product of the absolute value of any negative deferral amount in respect of the interest and the gross-up factor for the deferral amount.

Cost of participating interest

(12) Where a taxpayer's participating interest in a non-resident entity is disposed of by the taxpayer at a particular time in a taxation year and subsection (4) applies for the purpose of computing the taxpayer's income for the year in respect of the interest, for the purpose of determining the taxpayer's cost of the interest immediately before the particular time

(*a*) if the interest was held by the taxpayer at the beginning of the year, its cost to the taxpayer immediately before the particular time is deemed to be equal to the fair market value of the interest at the beginning of the year; and

(*b*) in any other case, its cost to the taxpayer immediately before the particular time is deemed to be equal to the amount that would be its cost to the taxpayer at the particular time if this Act were read without reference to this section (other than subsection (2)).

Deferral amount where same interest reacquired

(13) Subject to subsections (14) to (17), where a taxpayer disposes of a participating interest in an entity at any time in a taxation year of the taxpayer and subsection (4) applies for the purpose of computing the taxpayer's income for the year in respect of the interest, for the purpose

of applying subsection (4) to dispositions after that time the deferral amount of the taxpayer in respect of the interest is nil.

Fresh start re change of status of entity

(14) Where a participating interest is deemed by paragraph (11)(*a*) to have been acquired at a particular time by a taxpayer, for the purpose of applying subsection (4) to a subsequent disposition of the interest and a subsequent election in respect of the interest under clause (i)(C) of the description of D in paragraph (4)(*a*), the deferral amount of the taxpayer in respect of the interest shall

(*a*) for the purpose of clause (i)(C) of the description of B in the definition "deferral amount" in paragraph (1)(*b*), be determined as if subsection (4) had not applied to the taxpayer in respect of the interest for taxation years that began before the particular time; and

(*b*) be determined without reference to the application of subsection (13) with regard to dispositions that occurred before the particular time.

Fresh start after emigration of taxpayer

(15) Where a taxpayer ceases at a particular time to be resident in Canada, for the purpose of applying subsection (4) to dispositions, and elections under clause (i)(C) of the description of D in paragraph (4)(*a*), that occur or that are made after the particular time, the deferral amount in respect of the taxpayer's participating interests shall

(*a*) for the purpose of clause (i)(C) of the description of B in the definition "deferral amount" in paragraph (1)(*b*), be determined as if subsection (4) had not applied to the taxpayer in respect of participating interests for taxation years that began before the particular time; and

(*b*) be determined without reference to the application of subsection (13) with regard to dispositions that occurred before the particular time.

Fresh start re change of status of tax-exempt entity

(16) Where

(*a*) a taxpayer was not an exempt taxpayer for a particular taxation year, and

(*b*) the taxpayer is an exempt taxpayer for the following taxation year because of the application of paragraph (*b*) of the definition "exempt taxpayer" in subsection 94.1(1),

for the purpose of applying subsection (4) to dispositions, and elections under clause (i)(C) of the description of D in paragraph (4)(*a*), that occur or that are made after that following year, the deferral amount in respect of the taxpayer's participating interests shall

(*c*) for the purpose of clause (i)(C) of the description of B in the definition "deferral amount" in paragraph (1)(*b*), be determined as if subsection (4) had not applied to the taxpayer in respect of participating interests for taxation years that ended before that following year, and

(*d*) be determined without reference to the application of subsection (13) with regard to dispositions that occurred before that following year.

Superficial dispositions

(17) Where a taxpayer disposes of a particular participating interest in an entity, the deferral amount in respect of the particular interest would otherwise be a negative amount and the disposition would, if the particular interest were a capital property and a loss arose on the disposition, give rise to a superficial loss (within the meaning that would be assigned by section 54 if the definition "superficial loss" in that section were read without the reference to subsection 40(3.4) in paragraph (*h*) of that definition),

(*a*) except for the purpose of applying paragraph (*b*) in respect of the disposition, the deferral amount of the taxpayer in respect of the particular interest is deemed to be nil; and

(*b*) the deferral amount of the taxpayer in respect of the property that would be the substituted property referred to in that definition if the assumptions described in this subsection applied is deemed to be equal to the deferral amount of the taxpayer in respect of the particular interest.

Definitions and rules of application

94.3(1) The definitions in subsection 94.1(1), and paragraph 94.2(2)(*a*), apply in this section.

Prevention of double taxation

(2) Where at a particular time in a taxation year a taxpayer resident in Canada receives or becomes entitled to receive a payment from an entity in respect of a participating interest in the entity,

(*a*) there may be deducted in computing the taxpayer's income for the year the lesser of

(i) the amount, if any, by which

(A) the amount included (otherwise than because of subsection 94.2(4)) in computing the taxpayer's income for the year in respect of the payment,

exceeds

(B) the total of all amounts each of which is an amount deductible

(I) under subsection 91(5) in computing the taxpayer's income for the year in respect of the payment, or

(II) under section 113 in computing the taxpayer's taxable income for the year in respect of the payment, and

(ii) the amount, if any, by which

(A) the total of all amounts each of which is an amount added under subsection 94.1(3) or 94.2(4), in respect of the interest, in computing the taxpayer's income for the year or a preceding taxation year

exceeds the total of

(B) all amounts each of which is an amount deducted under subsection 94.1(3) or subsection 94.2(4), in respect of the interest, in computing the taxpayer's income for the year or a preceding taxation year, and

(C) all amounts each of which is an amount deducted under this paragraph, in respect of the interest, in computing the taxpayer's income in respect of a payment in respect of the interest that was received or became receivable before the particular time; and

(*b*) if the interest is capital property at the particular time, in computing the adjusted cost base to the taxpayer of the interest after the particular time there shall be deducted the amount deducted under paragraph (*a*) in computing the taxpayer's income.

(2) Subsection (1) applies to taxpayer's taxation years that begin after 2000, except that subsection 94.2(10) of the Act, as enacted by subsection (1), does not apply to taxation years that begin before 2002.

12. (1) The portion of subsection 95(1) of the Act before the definition "active business" is replaced by the following:

Definitions re foreign affiliates

95. (1) In this subdivision (other than sections 94 to 94.3),

(2) The portion of the definition "controlled foreign affiliate" in subsection 95(1) of the Act before paragraph (*a*) is replaced by the following:

"controlled foreign affiliate"
« société étrangère affiliée contrôlée »

"controlled foreign affiliate", at any time, of a taxpayer resident in Canada means a foreign affiliate of the taxpayer that is, at that time, a controlled foreign affiliate of the taxpayer because of subsection 94.1(12) or that is, at that time, controlled by

(3) The formula in the definition "foreign accrual property income" in subsection 95(1) of the Act is replaced by the following:

$$(A + A.1 + A.2 + B) - (D + E + F + G + H)$$

(4) The description of C in the definition "foreign accrual property income" in subsection 95(1) of the Act is repealed.

(5) Subparagraph (*a*)(i) of the definition "investment business" in subsection 95(1) of the Act is replaced by the following:

(i) a business carried on by it as a foreign bank, a trust company, a credit union, an insurance corporation or a trader or dealer in securities or commodities, the activities of which are regulated under the laws of the country in which the business is principally carried on, or

(6) The definition "relevant tax factor" in subsection 95(1) of the Act is replaced by the following:

"relevant tax factor"
« facteur fiscal
approprié »

"relevant tax factor" of a person or partnership for a taxation year means

(*a*) in the case of a corporation (or a partnership all the members of which, other than non-resident persons, are corporations), the quotient obtained when 1 is divided by the percentage set out in paragraph 123(1)(*a*) in respect of the year, and

(*b*) in any other case, 2.

(7) Subsection 95(2) of the Act is amended by adding the following after paragraph (g.1):

(*g*.2) in computing the foreign accrual property income of a particular foreign affiliate of a particular taxpayer for a particular taxation year of the particular affiliate, sections 94.1 to 94.3 shall apply as if

(i) the words "controlled foreign affiliate of the taxpayer" in paragraph (*a*) of the definition "exempt interest" in subsection 94.1(1) referred to a controlled foreign affiliate of the particular taxpayer and not to a controlled foreign affiliate of the particular affiliate,

(ii) subsection 94.1(3) were read without reference to the words "except where the taxpayer is non-resident at the end of the entity's year",

(iii) the form referred to in paragraph (*c*) of the description of A in subsection 94.1(5) in respect of participating interests in a foreign investment entity for a taxation year of the entity that ends in the particular year were required to be filed with, and only with, the particular taxpayer's return of income for the particular taxpayer's taxation year in which the particular year ends,

(iv) designations made by the particular taxpayer in the form referred to in subparagraph (iii) were made by the particular affiliate,

(v) the words "the particular taxpayer" in paragraph (*g*) of the description of A in subsection 94.1(5) referred to the particular taxpayer rather than to the particular affiliate,

(vi) each reference to "foreign affiliate" and "affiliate" in paragraph (*g*) of the description of A in subsection 94.1(5) were a reference to a foreign affiliate of the particular taxpayer and not to a foreign affiliate of the particular affiliate,

(vii) subsection 94.1(5) were read without reference to paragraph (*i*) of the description of A in subsection 94.1(5),

(viii) for the purpose of applying sections 94.1 and 94.2 in computing the income of a foreign investment entity in which the particular affiliate holds a participating interest,

(A) the words "controlled foreign affiliate of the taxpayer" in paragraph (*a*) of the definition "exempt interest" in subsection 94.1(1) referred to a controlled foreign affiliate of the particular taxpayer and not to a controlled foreign affiliate of the entity, and

(B) the fresh start year of the entity in respect of the particular affiliate were the first taxation year of the entity

(I) that ends in a taxation year of the particular affiliate that begins after 2000, and

(II) at any time in which both the particular affiliate holds a participating interest in the entity and the particular affiliate is a controlled foreign affiliate of the particular taxpayer,

(ix) an election under paragraph 94.1(4)(*a*) or clause (i)(C) of the description of D in paragraph 94.2(4)(*a*) for the particular year were required to be filed under that provision in respect of the particular affiliate, by, and only by, the particular taxpayer, with the Minister on or before the filing-due date of the particular taxpayer for the particular taxpayer's taxation year in which the particular year ends,

(x) section 94.2 were read without reference to subsection 94.2(5),

(xi) paragraph 94.2(1)(*b*) were read without reference to the words "at which the taxpayer was resident in Canada" and to clause (i)(B) of the description of B in that paragraph, and

(xii) the amount determined under paragraph 94.2(1)(*b*) did not include the portion of that amount that can reasonably be considered to have accrued during the period that the particular affiliate was not a foreign affiliate of any person described in any of subparagraphs (*f*)(iii) to (vii);

(8) Subsections (1) to (5) and (7) apply to taxation years of foreign affiliates of taxpayers that begin after 2000.

(9) Subsection (6) applies after 2000.

13. (1) Section 96 of the Act is amended by adding the following after subsection (1.8):

Application of sections 94.1 and 94.2

(1.9) Where an exempt taxpayer (as defined in subsection 94.1(1)) for a taxation year is a member of a partnership at any time in the year, for the purposes of applying paragraphs (1)(*f*) and (*g*) and 53(1)(*e*) and 2(*c*) to the taxpayer for a fiscal period of the partnership that ends in the year this Act shall be read without reference to sections 94.1 and 94.2.

(2) The portion of subsection 96(3) of the Act before paragraph (a) is replaced by the following:

Agreement or election of partnership members

(3) Where a taxpayer who was a member of a partnership at any time in a fiscal period has, for any purpose relevant to the computation of the taxpayer's income from the partnership for the fiscal period, made or executed an agreement, designation or election under or in respect of the application of any of subsections 13(4) and (16) and 14(6), section 15.2, subsections 20(9) and 21(1) to (4), section 22, subsection 29(1), section 34, clause 37(8)(*a*)(ii)(B), subsections 44(1) and (6), 50(1) and 80(5), (9), (10) and (11), section 80.04, subsections 94.1(4), (5) and (12), clause (i)(C) of the description of D in paragraph 94.2(4)(*a*), paragraph 95(2)(*g*.2) and subsections 97(2), 139.1(16) and (17) and 249.1(4) and (6) that, but for this subsection, would be a valid agreement, designation or election,

(3) Subsection 96(9) of the Act is replaced by the following:

Application of foreign partnership rule

(9) For the purposes of applying subsection (8) and this subsection,

(*a*) where it can reasonably be considered that one of the main reasons that a member of a partnership is resident in Canada is to avoid the application of subsection (8), the member is deemed not to be resident in Canada; and

(*b*) where at any time a particular partnership is a member of another partnership,

(i) each person or partnership that is, at that time, a member of the particular partnership is deemed to be a member of the other partnership at that time,

(ii) each person or partnership that becomes a member of the particular partnership at that time is deemed to become a member of the other partnership at that time, and

(iii) each person or partnership that ceases to be a member of the particular partnership at that time is deemed to cease to be a member of the other partnership at that time.

(4) Subsections (1) to (3) apply to fiscal periods that begin after ANNOUNCEMENT DATE.

14.(1) The portion of subsection 104(1.1) of the Act before paragraph (*a*) is replaced by the following:

Restricted meaning of beneficiary

(1.1) For the purposes of subsection (1), subparagraph 73(1.02)(*b*)(ii), paragraph (*b*) of the definition "resident beneficiary" in subsection 94(1), and paragraph 107.4(1)(*e*), a person or partnership is deemed not to be a beneficiary under a trust at a particular time where the person or partnership is beneficially interested in the trust at the particular time solely because of

(2) Section 104 of the Act is amended by adding the following after subsection (4):

Mark-to-market property

(4.1) Notwithstanding any other provision of this Act, the determination of whether property is capital property for the purpose of subsection (4) shall be made without reference to subparagraph 39(1)(*a*)(ii.3) and section 94.2.

(3) The portion of subsection 104(6) of the Act before paragraph (*a*) is replaced by the following:

Deduction in computing income of trust

(6) Subject to subsections (7) and (7.01), for the purposes of this Part, there may be deducted in computing the income of a trust for a taxation year

(4) Section 104 of the Act is amended by adding the following after subsection (7):

Trusts deemed to be resident in Canada

(7.01) Where a trust is deemed by subsection 94(3) to be resident in Canada for a taxation year for the purpose of computing the trust's income for the year, the maximum amount deductible under subsection (6) in computing its income for the year is deemed to be the amount, if any, by which

(*a*) the maximum amount that, but for this subsection, would be deductible under subsection (6) in computing its income for the year,

exceeds the lesser of

(*b*) the total of

(i) the designated income of the trust for the year (within the meaning assigned by subsection 210.2(2)), and

(ii) all amounts each of which is 50% of an amount paid or credited in the year to the trust that would, if this Act were read without reference to subparagraph 94(3)(*a*)(iii) and sections 216 and 217, be an amount as a consequence of the payment or crediting of which the trust would have been liable to tax under Part XIII, and (*c*) the amount, if any, by which

(i) the maximum amount that, but for this subsection, would be deductible under subsection (6) in computing its income for the year

exceeds

(ii) the maximum amount that would be deductible in computing its income for the year if this section were read without reference to this subsection and if the only amounts that became payable in the year to a beneficiary were amounts that became payable in the year to

(A) a partnership (other than a partnership that is a Canadian partnership on the day that would be determined under paragraph 214(3)(*f*) in respect of the amount if the assumptions set out in subparagraph (*b*)(ii) applied), or

(B) a non-resident person on the day that would be determined under paragraph 214(3)(*f*) in respect of the amount if the assumptions set out in subparagraph (*b*)(ii) applied.

(5) Paragraph 104(21.3)(*a*) of the Act is replaced by the following:

(*a*) the total of all amounts each of which is an allowable capital loss (other than an allowable business investment loss) of the trust for the year from the disposition of a capital property, and

(6) Subsection 104(24) of the Act is replaced by the following:

Amount payable

(24) For the purposes of subparagraph 53(2)(*h*)(i.1) and subsections (6), (7), (7.01), (13) and (20), an amount is deemed not to have become payable to a beneficiary in a taxation year unless it was paid in the year to the beneficiary or the beneficiary was entitled in the year to enforce payment of it.

(7) Subsections (1) to (6) apply to trust taxation years that begin after 2000.

15. (1) The portion of subsection 108(3) of the Act before paragraph (*a*) is replaced by the following:

Income of a trust in certain provisions

(3) For the purposes of the definition "income interest" in subsection (1) and the definition "exempt foreign trust" in subsection 94(1), the income of a trust is its income computed without reference to the provisions of this Act and, for the purposes of the definition "pre-1972 spousal trust" in subsection (1) and paragraphs 70(6)(*b*) and (6.1)(*b*), 73(1.01)(*c*) and 104(4)(*a*), the income of a trust is its income computed without reference to the provisions of this Act, minus any dividends included in that income

(2) Subsection (1) applies to taxation years that begin after 2000.

16. (1) Clause 113(1)(*b*)(i)(A) of the Act is replaced by the following:

(A) the corporation's relevant tax factor for the year,

(2) Clause 113(1)(*c*)(i)(B) of the Act is replaced by the following:

(B) the corporation's relevant tax factor for the year,

(3) Subsections (1) and (2) apply after 2000.

17. (1) The portion of section 114 of the Act before paragraph (a) is replaced by the following:

Individual resident in Canada for only part of year

114. Notwithstanding subsection 2(2), subject to subsection 94.2(5) the taxable income for a taxation year of an individual who is resident in Canada throughout part of the year and non-resident throughout another part of the year is the amount, if any, by which

(2) Subsection (1) applies to the 2001 and subsequent taxation years.

18. (1) Subsection 122(2) of the Act is amended by striking out the word "and" at the end of paragraph (*d*) and by adding the following after paragraph (*d*):

(*d*.1) was not a trust to which a contribution, within the meaning assigned by section 94, was made after **ANNOUNCEMENT DATE**; and

(2) Subsection (1) applies to taxation years that begin after 2000.

19. (1) Paragraph 149(10)(*c*) of the Act is replaced by the following:

(*c*) for the purposes of applying sections 37, 65 to 66.4, 66.7, 94.1 to 94.3, 111 and 126, subsections 127(5) to (35) and section 127.3 to the corporation, the corporation is deemed to be a new corporation the first taxation year of which began at that time; and

(2) Subsection (1) applies to each corporation that, after 2000, becomes or ceases to be exempt from tax on its taxable income under Part I of the Act.

20. (1) Paragraph (*d*) of the description of A in subsection 162(10.1) of the Act is replaced by the following:

(*d*) where the return is required to be filed under section 233.2 in respect of a trust, 5% of the total of all amounts each of which is the fair market value, at the time it was made, of a contribution of the person or partnership made to the trust before the end of the last taxation year of the trust in respect of which the return is required,

(2) Section 162 of the Act is amended by adding the following after subsection (10.1):

Application to trust contributions

(10.11) Subsections 94(1) and (2) apply for the purpose of paragraph (*d*) of the description of A in subsection (10.1), except that for this purpose the definition "arm's length transfer" in subsection 94(1) shall be read without reference to subparagraph (*a*)(v) of that definition.

(3) The portion of subsection 162(10.3) of the Act before paragraph (*a*) is replaced by the following:

Application to partnerships

(10.3) For the purposes of paragraph (*f*) of the description of A in subsection (10.1) and subsection (10.2), in determining whether a non-resident corporation is a foreign affiliate or a controlled foreign affiliate of a partnership,

(4) Subsection 162(10.4) of the Act is repealed.

(5) Subsections (1) to (3) apply to returns in respect of taxation years that begin after 2000.

21. (1) Paragraph 163(2.4)(*b*) of the Act is replaced by the following:

(*b*) where the return is required to be filed under section 233.2 in respect of a trust, the greater of

(i) $24,000, and

(ii) 5% of the total of all amounts each of which is the fair market value, at the time it was made, of a contribution of the person or partnership made to the trust before the end of the last taxation year of the trust in respect of which the return is required;

(2) Section 163 of the Act is amended by adding the following after subsection (2.4):

Application to trust contributions

(2.41) Subsections 94(1) and (2) apply for the purpose of subparagraph (*b*)(ii), except that for this purpose the definition "arm's length transfer" in subsection 94(1) shall be read without reference to subparagraph (*a*)(v) of that definition.

(3) The portion of subsection 163(2.6) of the Act before paragraph (*a*) is replaced by the following:

Application to partnerships

(2.6) For the purposes of paragraph (2.4)(*d*) and subsection (2.5), in determining whether a non-resident corporation is a foreign affiliate or a controlled foreign affiliate of a partnership,

(4) Subsection 163(2.91) of the Act is repealed.

(5) Subsections (1) to (4) apply to returns in respect of taxation years that begin after 2000.

22. (1) The definitions "specified beneficiary" and "specified foreign trust" in subsection 233.2(1) of the Act are repealed.

(2) Subsections 233.2(2) and (3) of the Act are replaced by the following:

Rule of application

(2) Subsections 94(1) and (2) apply for the purposes of this section (other than paragraph (4.1)(*b*)) and paragraph 233.5(*c*.1), except that for these purposes the definition "arm's length transfer" in subsection 94(1) shall be read without reference to subparagraph (*a*)(v) of that definition.

(3) Subsection 233.2(4) of the Act is replaced by the following:

Filing information on foreign trusts

(4) Where

(*a*) a contribution has been made by a person to a particular trust (other than an exempt trust or a trust described in any of paragraphs (*c*) to (*i*) of the definition "exempt foreign trust" in subsection 94(1)) at any time in a taxation year of the particular trust or in a preceding taxation year,

(*b*) the person is

(i) resident in Canada at the end of the particular trust's taxation year, and

(ii) not, at the end of the year,

(A) a mutual fund corporation,

(B) a non-resident-owned investment corporation,

(C) a person (other than a trust) all of whose taxable income for the person's taxation year that includes that time is exempt from tax under Part I,

(D) a trust all of the taxable income of which for its taxation year that includes that time is exempt from tax under Part I,

(E) a mutual fund trust,

(F) a trust described in any of paragraphs (*a*) to (*e*.1) of the definition "trust" in subsection 108(1),

(G) a registered investment,

(H) a trust in which all persons beneficially interested are persons described in clauses (A) to (G), or

(I) a person who is a contributor to the particular trust only because of being a contributor to a trust described in any of clauses (D) to (H), and

(*c*) the particular trust is not resident in Canada at the end of its taxation year,

the person shall file an information return in prescribed form, in respect of the particular trust's taxation year, with the Minister on or before the person's filing-due date for the person's taxation year in which the particular trust's taxation year ends.

Similar arrangements

(4.1) Where

(*a*) property is at any time, directly or indirectly, transferred or loaned by a person to be held

(i) under an arrangement governed by laws that are not laws of Canada or a province, or

(ii) by a non-resident entity (within the meaning assigned by subsection 94.1(1)),

(*b*) the transfer or loan would not be an arm's length transfer (within the meaning assigned by the definition "arm's length transfer" in subsection 94(1) if that definition were read without reference to the words "in respect of a trust" and to subparagraph (*a*)(v)),

(*c*) the transfer or loan is not solely in exchange for property that would be described in paragraphs (*a*) to (*i*) of the definition "specified foreign property" in subsection 233.3(1) if that definition were read without reference to paragraphs (*j*) to (*q*), (*d*) the entity or arrangement is not a trust in respect of which the person would, but for this subsection, be required to file an information return for a taxation year that includes that time, and

(*e*) the entity or arrangement is not an exempt foreign trust (within the meaning assigned by subsection 94(1)) or an exempt trust,

for the purposes of this section and sections 162, 163 and 233.5, the person's obligations under subsection (4) (except to the extent that they are waived in writing by the Minister) shall be determined as if the transfer were a contribution to which paragraph (4)(*a*) applied, the entity or arrangement were a trust not resident in Canada throughout the calendar year that includes that time and the taxation year of the entity or arrangement were that calendar year.

(4) Subsections (1) to (3) apply to returns in respect of taxation years that begin after 2000.

23. (1) Paragraph (*d*) of the definition "specified foreign property" in subsection 233.3(1) of the Act is replaced by the following:

(*d*) an interest in a non-resident trust or in a trust that, but for subparagraph 94(3)(*a*)(ii), would be non-resident,

(2) The definition "specified foreign property" in subsection 233.3(1) of the Act is amended by adding the following after paragraph (*d*):

(*d*.1) an interest in an insurance policy that is deemed by subsection 94.2(10) to be a participating interest in a non-resident entity,

(3) Paragraph (*l*) of the definition "specified foreign property" in subsection 233.3(1) of the Act is repealed.

(4) Paragraph (*m*) of the definition "specified foreign property" in subsection 233.3(1) of the Act is replaced by the following:

(*m*) an interest in a non-resident trust (or in a trust that, but for subparagraph 94(3)(*a*)(ii), would be non-resident) that was not acquired for consideration by the person or partnership or by a person related to the person or partnership,

(5) Subsections (1), (3) and (4) apply to interests in a trust held at any time in taxation years of the trust that begin after 2000.

(6) Subsection (2) applies to returns for taxation years that begin after 2001.

24. (1) Subsection 233.4(1) of the Act is amended by adding the word "and" at the end of paragraph (*a*) and by repealing paragraph (*b*).

(2) Subparagraph 233.4(1)(*c*)(ii) of the Act is replaced by the following:

(ii) of which a non-resident corporation is a foreign affiliate at any time in the fiscal period.

(3) The portion of subsection 233.4(2) of the Act before paragraph (*a*) is replaced by the following:

Rules of application

(2) For the purpose of this section, in determining whether a non-resident corporation is a foreign affiliate or a controlled foreign affiliate of a taxpayer resident in Canada or of a partnership

(4) Subsections (1) to (3) apply to taxation years and fiscal periods that begin after 2000.

25. (1) Paragraph 233.5(*c*) of the Act is replaced by the following:

(*c*) if the return is required to be filed under section 233.2 in respect of a trust, at the time of each transaction, if any, entered into by the person or partnership after March 5, 1996 and before **[ANNOUNCEMENT DATE + 1]** that gave rise to the requirement to file a return for a taxation year of the trust that began before 2001 or that affects the information to be reported in the return, it was reasonable to expect that sufficient information would be available to the person or partnership to comply with section 233.2 in respect of each taxation year of the trust that began before 2001;

(*c*.1) if the return is required to be filed under section 233.2, at the time of each contribution (determined with reference to subsection 233.2(2)) made by the person or partnership after **ANNOUNCEMENT DATE** that gives rise to the requirement to file the return or that affects the information to be reported in the return, it was reasonable to expect that sufficient information would be available to the person or partnership to comply with section 233.2;

(*c*.2) if the return is required to be filed under section 233.4 by a person or partnership in respect of a corporation that is a controlled foreign affiliate, for the purpose of that section, of the person or partnership, at the time of each transaction, if any, entered into by the person or partnership after March 5, 1996 that gives rise to the requirement to file the return or that affects the information to be reported in the return, it was reasonable to expect that sufficient information would be available to the person or partnership to comply with section 233.4; and

(2) Subsection (1) applies to returns required to be filed for taxation years that begin after 2000.

26. (1) The definition "cost amount" in subsection 248(1) of the Act is amended by adding the following after paragraph (*c*.1):

(*c*.2) where the cost at that time to the taxpayer of the property is determined under subsection 94.2(12), the cost so determined,

(2) The definition "inventory" in subsection 248(1) of the Act is replaced by the following:

"inventory"
« inventaire »

"inventory" means a description of property (other than property to which subsection 94.2(3) applies) the cost or value of which is relevant in computing a taxpayer's income from a business for a taxation year or would have been so relevant if the income from the business had not been computed in accordance with the cash method and, with respect to a farming business, includes all of the livestock held in the course of carrying on the business;

(3) Subsection 248(1) of the Act is amended by adding the following in alphabetical order:

"foreign accrual property income"
« revenu étranger accumulé, tiré de biens »

"foreign accrual property income" has the meaning assigned by section 95;

"non-discretionary trust"
« fiducie non discrétionnaire »

"non-discretionary trust" has the meaning assigned by subsection 17(15).

(4) Subsections (1) and (3) apply after 2000.

(5) Subsection (2) applies to fiscal periods that begin after 2000.

Explanatory Notes

PREFACE

These explanatory notes describe, for discussion purposes, proposed amendments to the *Income Tax Act*. The proposed amendments are described, clause by clause, for the assistance of Members of Parliament, taxpayers and their professional advisors.

The Honourable Paul Martin
Minister of Finance

These explanatory notes are provided to assist in an understanding of proposed amendments to the *Income Tax Act*. These notes are intended for information purposes only and should not be construed as an official interpretation of the provisions they describe.

Clause 1

ITA
12(1)(*k*)

Section 12 of the *Income Tax Act* provides for the inclusion of various amounts in computing a taxpayer's income for a taxation year from business or property. Paragraph 12(1)(*k*) refers to certain amounts required by existing sections 90 to 95 to be so added.

Paragraph 12(1)(*k*) is amended so that it refers to all amounts required to be added in computing income under amended sections 90 to 95, including new sections 94 to 94.2.

This amendment applies to taxation years that begin after 2000.

Clause 2

ITA
17(15)

Subsection 17(15) of the Act defines expressions that apply for the purposes of section 17, which provides rules under which imputed interest, in connection with debt owing to a taxpayer from a non-resident person, is included in computing the taxpayer's income. The expression "controlled foreign affiliate" is defined to have the same meaning as it does under subsection 95(1) of the Act, except that for the purpose of section 17 a non-resident corporation must be controlled by Canadian residents in order to be treated as a controlled foreign affiliate of a taxpayer resident in Canada.

The definition "controlled foreign affiliate" in subsection 17(15) is amended so that new subsection 94.1(12) does not apply for the purposes of section 17. Under that new subsection, an election is available so that a foreign affiliate of a taxpayer is treated as a controlled foreign affiliate of the taxpayer.

This amendment applies after 2000.

Clause 3

ITA
39(1)(*a*)(ii.3)

Paragraph 39(1)(*a*) of the Act contains a description of a taxpayer's capital gain for a taxation year from the disposition of property. This paragraph provides that gains from dispositions of specified properties are to be excluded in determining a capital gain. Under subparagraph 39(1)(*a*)(ii.2), the specified properties include specified debt obligations, where subsection 142.4(4) or (5) applies to the disposition, and mark-to-market properties where subsection 142.5(1) applies to the disposition. Under subparagraph 39(1)(*b*)(ii), the same exclusion generally applies with regard to a taxpayer's capital loss.

New subparagraph 39(1)(*a*)(ii.3) provides a similar exclusion for property in respect of which new subsection 94.2(3) applies to a taxpayer immediately before the time of the disposition. Subsection 94.2(3) sets out the conditions for the application of the mark-to-market taxation regime under subsection 94.2(4) for participating interests in foreign investment entities. Because of paragraph 94.2(5)(*b*), this exclusion does not apply where the taxpayer is not resident in Canada immediately before the time of the disposition.

This amendment applies to dispositions that occur after 2000.

Clause 4

ITA
53(1)(*d*.1)

Paragraph 53(1)(*d*.1) of the Act, applied together with existing paragraph 94(5)(*a*), provides for an addition in computing the adjusted cost base (ACB) to a taxpayer of the taxpayer's capital interest in a trust to which existing paragraph 94(1)(*d*) applies. It is amended to ensure that historical ACB additions are maintained, notwithstanding the replacement of the rules in existing section 94.

This amendment applies after 2000.

ITA
53(1)(*m*) and (*m*.1)

Paragraph 53(1)(*m*) of the Act provides for an addition in computing the ACB to a taxpayer of "offshore investment fund property" to which existing section 94.1 applies. It is amended to ensure that the historical ACB additions are maintained, notwithstanding the replacement of the rules in existing section 94.1.

Paragraph 53(1)(*m*.1) is introduced to provide for the ACB additions contemplated by new subsections 94.1(9) and 94.2(11). For more detail, see the commentary on those subsections.

These amendments apply after 2000.

ITA
53(2)(*w*)

Paragraph 53(2)(*w*) of the Act is introduced to provide for the ACB reductions contemplated by new subsections 94.1(9), 94.2(11) and 94.3(2). For more detail, see the commentary on those subsections.

New paragraph 53(1)(*w*) applies after 2000.

Clause 5

ITA
70(3.1)

Under subsection 70(2) of the Act, the value of certain "rights or things" owned by an individual at death is required to be included in the individual's income for the year of death. Subsection 70(3) provides that this rule does not apply in connection with "rights or things" transferred to beneficiaries of the deceased within a specified time. Subsection 70(3.1) provides that certain property does not constitute a "right or thing" for this purpose.

Subsection 70(3.1) is amended so that a "right or thing" also does not include property in respect of which new subsection 94.2(3) applied to the deceased immediately before death. New subsection 94.2(3) sets out the conditions for the application of the mark-to-market taxation regime under subsection 94.2(4) for participating interests in foreign investment entities.

This amendment applies to the 2001 and subsequent taxation years.

ITA
70(5.2)(*e*)

Subsection 70(5.2) of the Act provides rules with respect to the disposition of resource properties and land inventories on death.

Paragraph 70(5.2)(*e*) is introduced to provide for a deemed disposition, on the death of an individual, of an interest in a foreign investment entity held by the individual. Paragraph 70(5.2)(*e*) applies only to interests in foreign investment entities in respect of which new subsection 94.2(3) applied to the deceased immediately before death. (New subsection 94.2(3) sets out the conditions for the application of the mark-to-market taxation regime under subsection 94.2(4) for participating interests in foreign investment entities.)

A disposition under paragraph 70(5.2)(*e*) is deemed to occur at the fair market value of an interest in a foreign investment entity and to be acquired for the same amount by a person who acquires the interest as a consequence of the individual's death. The proceeds of disposition are included in the value of A in the formula in paragraph 94.2(4)(*a*) in computing the deceased's income under subsection 94.2(4) for the taxation year of death. The deceased is treated as not having held the interest after death.

This amendment applies to the 2001 and subsequent taxation years.

Clause 6

ITA
75(3)(*c*.2)

Subsection 75(2) of the Act generally provides that, where a person transfers property to a trust under certain conditions, the income from the property is attributed to the person. Subsection 75(3) exempts certain trusts from this attribution rule.

Subsection 75(3) is amended so that it does not apply to a trust that is not resident in Canada for the purposes of computing its income, notwithstanding that there is a person who is, at the end of the year, both resident in Canada and a contributor (as defined in section 94) to the trust. In effect, this exception will generally apply to trusts in respect of which the contributors are recent immigrants to Canada (i.e., resident in Canada for not more than 60 months). The exception is consistent with similar 60-month exemptions in:

- section 94 (see the definition of "resident contributor" in subsection 94(1) and subsection 94(3)),
- section 94.1 (see paragraph 94.1(2)(*a*)), and
- section 94.2 (see subparagraph 94.2(3)(*b*)(*i*)).

This amendment applies to trust taxation years that begin after 2000.

Clause 7

ITA
85(1.1)(*g*)

Subsection 85(1.1) of the Act describes the types of property (which are referred to as "eligible property") that may be transferred to a corporation under subsection 85(1). Eligible property includes certain capital property described in the subsection, as well as additional property.

Subsection 85(1.1) is amended so that eligible property for a taxpayer, in all cases, excludes property in respect of which new subsection 94.2(3) applies to the taxpayer. New subsection 94.2(3) sets out the conditions for the application of the mark-to-market taxation regime under subsection 94.2(4) for participating interests in foreign investment entities.

This amendment applies after 2000.

Clause 8

ITA
87(2)(*j*.95)

Section 87 of the Act sets out rules that apply on the amalgamation of two or more taxable Canadian corporations. The amalgamated corporation is generally treated as a continuation of the predecessor corporations for the purposes of the Act.

New paragraph 87(2)(*j*.95) provides that, where there has been an amalgamation of two or more taxable Canadian corporations, the amalgamated corporation is deemed to be a continuation of its predecessor corporations for the purposes of sections 94 to 94.3, which relate to foreign trusts and foreign investment entities. Thus, for example, an amalgamated corporation will be considered to be a "contributor" to a trust (as defined in subsection 94(1)) if any predecessor corporation was a contributor to the trust. In addition, the new corporation's "deferral amount" under paragraph 94.2(1)(*b*) in respect of an interest in a foreign investment entity will be determined in the same manner as a predecessor's "deferral amount" in respect of the same interest.

Because of the operation of paragraph 88(1)(*e*.2), new paragraph 87(2)(*j*.95) also applies to windings-up to which section 88 applies.

This amendment applies after 2000.

Clause 9

ITA
91(1)

Subsection 91(1) of the Act provides that a taxpayer who is resident in Canada must include in computing income an amount in respect of each share owned by the taxpayer in the capital stock of a controlled foreign affiliate of the taxpayer.

Subsection 91(1) is amended so that it does not result in additional income for a taxpayer arising because of the ownership by the taxpayer (or a controlled foreign affiliate of the taxpayer) of shares that are "tracked interests" subject to the mark-to-market regime in section 94.2 by reason of the application of subsection 94.2(9). Note that, because of paragraph (*a*) of the definition "exempt interest" in subsection 94.1(1), a share of the capital stock of a controlled foreign affiliate is otherwise not subject to the regime for foreign investment entities in sections 94.1 and 94.2.

This amendment applies to trust taxation years that begin after 2000.

ITA
91(4)

Subsection 91(4) of the Act provides for a deduction in computing the income of a taxpayer resident in Canada. The deduction is available to a taxpayer where the taxpayer has included an amount under subsection 91(1) in computing income in respect of a share of the capital stock of a controlled foreign affiliate of the taxpayer. The deduction is generally determined with reference to foreign taxes payable by the affiliate and a "relevant tax factor". The "relevant tax factor" for a resident taxpayer is designed to permit a deduction for the resident taxpayer to result in tax relief that is representative of foreign taxes payable by a controlled foreign affiliate of the resident taxpayer.

Subsection 91(4) is amended to explicitly link the "relevant tax factor" to the resident taxpayer and the taxation year for which the deduction under subsection 91(4) is claimed. This is consistent with the more explicit definition of "relevant tax factor" described below in the commentary on subsection 95(1).

This amendment applies after 2000.

Clause 10

ITA
94

OVERVIEW

Existing Rules

Section 94 of the Act sets out rules that tax the passive income earned by certain non-resident trusts. Section 94 generally applies if a person resident in Canada has transferred or loaned property to a non-resident trust that has one or more beneficiaries who are resident in Canada.

Section 94 uses two different methods to impose tax, depending on whether or not the trust is discretionary. A discretionary trust is a trust under which a person has a discretionary power to determine the amount of the income or capital of the trust that one or more beneficiaries will receive.

If the non-resident trust is discretionary, paragraph 94(1)(*c*) deems the trust to be resident in Canada for the purposes of Part I of the Act and deems its income for tax purposes to be the total of its Canadian source income and its foreign accrual property income, if any. Each beneficiary is jointly and severally liable to pay the Canadian tax of the trust. However, the liability can be enforced against a particular beneficiary only to the extent that the beneficiary has received a distribution from the trust or proceeds from the sale of an interest in the trust.

If the non-resident trust is not a discretionary trust, paragraph 94(1)(*d*) provides that it is to be treated in much the same manner that a non-resident corporation is treated. If a Canadian resident beneficiary holds an interest in the trust with a fair market value equal to 10% or more of the total fair market value of all interests in the trust, the trust is deemed to be a controlled foreign affiliate of the beneficiary. Consequently, the foreign accrual property income rules apply to the trust and the beneficiary, requiring the beneficiary to include a portion of the foreign accrual property income of the trust in income. On the other hand, beneficiaries that do not have 10% or greater interests in the trust may be subject to tax under the offshore investment fund rules in section 94.1. If section 94.1 does not apply, such beneficiaries are taxed only if trust income becomes payable to them in the year that it arises.

New Rules

New section 94 takes a different approach to the taxation of non-resident trusts (NRTs) that bears some similarity to the grantor trust approach used by the United States, New Zealand and Australia. In general, if a Canadian resident contributes property to a non-resident trust, the contributor, the non-resident trust and certain Canadian resident beneficiaries of the trust may all become liable to pay Canadian tax on the world-wide income of the trust.

Except as indicated otherwise, the amendments to section 94 apply to taxation years of trusts that begin after 2000. The table below briefly summarizes section 94 and related rules.

Issue	Summary	References
1. Which trusts are subject to the new NRT rules?	A. In general, a trust (other than an exempt foreign trust) will be subject to tax for a taxation year as a trust resident in Canada if a contribution was made to the trust by a person who is resident in Canada at the end of the year (other than a recent immigrant to Canada).	S. 94(3) "exempt foreign trust" -- s. 94(1) "contribution" – s. 94(1) and (2) "resident contributor" – s. 94(1) As to 60-month test for new immigrants, see definition "resident contributor" in s. 94(1).
	B. In addition, a trust (other than an exempt foreign trust) will generally be subject to Canadian tax for a taxation year if • the contribution was made by a person when the person was resident in Canada (or within a 60-month period before the person became resident in Canada or within a 60-month period after the person ceased to be resident in Canada), • by the end of the year that person had been resident in Canada for more than 60 months, and • at the end of the year there is a person resident in Canada who is beneficially interested in the trust.	S. 94(3) "contribution" – s. 94(1) "connected contributor" – s. 94(1) "resident beneficiary" – s. 94(1)

Issue	Summary	References
2. Who is responsible for the tax payable an NRT?	The trust is required to pay tax. If it fails to do so, each contributor referred to in 1(A) and/or each beneficiary referred to in 1(B) is jointly and severally liable with the trust for the tax. However, the amount recoverable from a person who is simply a beneficiary is limited to benefits received by the beneficiary from the trust. Relief is also available in some cases for a contributor whose contribution to the trust is insignificant relative to other contributions made to the trust.	Joint liability: paragraph 94(3)(*d*) Relief from joint liability: s. 94(7) 10% and $10,000 tests for significant contribution: paragraph 94(7)(*b*).
3. Where the NRT rules do apply for a taxation year to a trust, how will the trust's tax liabilities be calculated?	A. Canadian rules apply to the trust as if the trust were resident in Canada throughout the year for the purpose of computing the trust's income.	s. 94(3)
	B. Explicit rule treats the trust as becoming resident in Canada, with resulting adjustment to cost amount of property under section 128.1.	s. 94(3)(*c*)
	C. Parts XII.2 and XIII do not apply to the trust. Explicit exemption from Part XIII tax on amounts distributed to the trust, although payer must still withhold.	s. 94(3)(*a*)(iii) and (4)(*d*)
	D. Flow-through of income to resident and non-resident beneficiaries permitted, subject to special rules in the event that Canadian-source income is distributed to non-residents.	s. 104(7.01) - special rules

ITA
94(1)

New subsection 94(1) of the Act defines a number of expressions that apply for the purpose of section 94.

"accounting profit"

The "accounting profit" of a trust for a taxation year refers to the trust's profit for the year (determined before taking into account income or profits tax) reflected in its financial statements, on the assumption that the financial statements were prepared in accordance with accounting principles substantially similar to generally accepted accounting principles used in Canada. Where such financial statements have not been prepared, a trust's "accounting profit" for a taxation year is the amount that would be the trust's total profit (determined before taking into account income or profits tax) for the year, from businesses carried on by the trust and properties owned by the trust, if that amount were calculated in accordance with generally accepted accounting principles used in Canada.

This definition is used only in paragraph (*d*) of the definition "exempt foreign trust", as described in the commentary below.

"arm's length transfer"

An "arm's length transfer" does not result in any person or partnership being considered to be a "contributor" to a trust. Accordingly, subsection 94(3) does not apply to a non-resident trust as a consequence only of an arm's length transfer.

An "arm's length transfer" is, in general terms:

- a transfer or loan that is part of an arm's length exchange[1],
- an arm's length return on an investment, conferred by the entity in which the investment is made[2],

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[1] Subparagraph (*a*)(i) of the definition.
[2] Subparagraph (*a*)(ii) of the definition.

- a repayment of an arm's length loan[3],
- a transfer or loan made in the ordinary course of business[4], or
- a transfer or loan that was not undertaken to allow for the conferral, in the future, of a benefit on the transferor, on a descendant of the transferor or on any person with whom the transferor or descendant does not deal at arm's length[5].

However, a transfer or loan qualifies as an "arm's length transfer" in respect of a trust only where it is reasonable to conclude that none of reasons for the transfer or loan included the relationship between the maker of the transfer or loan and any person or partnership that was

- beneficially interested in the trust,
- a trustee of the trust,
- a person having influence over the operation of the trust or the enforcement of its terms, or
- a person having influence over the selection or appointment of other persons so described.

It should be noted that, under amended subsection 233.2(4) and new subsection 233.2(4.1), an "arm's length transfer" covered by subparagraph (*a*)(v) of the definition cannot be used as a basis for an exemption from the reporting requirements under those subsections. Reporting requirements under those subsections are structured in this way so that claims for relief on the basis of paragraph (*a*)(*v*) of the definition "arm's length transfer" can be carefully scrutinized by the Canada Customs and Revenue Agency (CCRA).

Reference should also be made to new subsection 94(2), which provides various rules that have the effect of broadening the meaning of a "transfer" of property.

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[3] Subparagraph (*a*)(iii) of the definition.

[4] Subparagraph (*a*)(iv) of the definition.

[5] Subparagraph (*a*)(v) of the definition.

"connected contributor"

Where a person is a "connected contributor" to a trust, it can result in another person being a "resident beneficiary" under a non-resident trust. A "resident beneficiary" under a non-resident trust can, to an extent, be liable for the trust's income tax, as set out in greater detail on the commentary on subsections 94(3) and (7).

A "connected contributor" at any time is any person, living or deceased, who is a "contributor" to the trust (as defined in new subsection 94(1)) at that time, provided that the person:

- is not, or at the time of death was not, a recent immigrant to Canada (i.e., an individual who was resident in Canada for a period of, or periods the total of which is, not more than 60 months), or

- is not a person who is a "contributor" only because of one or more transactions that occurred at a "non-resident time" of the contributor.

For these purposes, a "non-resident time" is defined within the definition "connected contributor" as being a particular time at which a contributor is non-resident, provided that the contributor is also non-resident (or not in existence) throughout the period that began 60 months before the particular time and ends 60 months after the particular time. However, if the particular time occurs before **[ANNOUNCEMENT DATE + 1]** or the trust arose on and as a consequence of the death of the person, the period begins 18 months (rather than 60 months) before the particular time, consistent with existing subclause 94(1)(*b*)(i)(A)(II).

"contribution"

Where a "contribution" is made to a non-resident trust by a person, that person is a "contributor" who, in certain cases, can be jointly and severally liable under subsection 94(3) for the trust's income taxes.

A transferor is considered to make a "contribution" to a trust where a property is transferred or loaned to the trust and any one of three alternative sets of conditions is satisfied. The three sets of conditions are described below.

First, a transfer or loan of a particular property at any time to a trust is considered to be a contribution at that time by a person or partnership to a trust where:

- the particular property is, at that time, transferred, or loaned, directly to the trust by the person or partnership; and
- the transfer or loan is not an "arm's length transfer" (as described in the commentary above).

The second and third alternate sets of conditions deal with cases where a particular person or partnership can be viewed as indirectly contributing property to a trust because of a loan or transfer of property (or an obligation to transfer or loan property) to another person or partnership (other than the trust). In such circumstances, property contributed at a particular time in the same series of transactions and events by another person or partnership to a trust will be treated as having been contributed at the particular time by the particular person or partnership to the trust.

More specifically, the second alternate set of conditions deals with the case where a particular transfer or loan of a property (other than an arm's length transfer) is made by a particular person or partnership as part of a series of transactions or events that includes another transfer or loan of any property, to the particular trust, by another person or partnership. The other transfer or loan is a considered to be a "contribution" to the particular trust by the particular person or partnership to the extent that the other transfer or loan can reasonably be considered to have been enabled by the particular transfer or loan. The contribution is considered to be made at the time of the other transfer or loan.

The third alternate set of conditions deals with the case where a particular person or partnership becomes obligated to make a particular transfer or loan of a property (other than in an arm's length transfer) as part of a series of transactions or events that includes another transfer or loan of any property, to the particular trust, by another person or partnership. The other transfer or loan is considered to be a "contribution" by the particular person or partnership to the particular trust to the extent that the other transfer or loan can reasonably be considered to have been enabled by the particular person's obligation to make the particular loan or transfer.

The contribution is considered to be made at the time of the other transfer or loan.

Under new subsection 94(2), there are a number of rules that have the effect of applying the definition "contribution" more broadly than would otherwise be the case. For example, the rendering of services is generally treated as a transfer of property. An obligation to render services is likewise treated as an obligation to transfer property. For more details, see the commentary on subsection 94(2).

As noted earlier, this definition applies to taxation years of trusts that begin after 2000, whether or not a relevant transfer or loan occurred before that time. However, in order to provide for transition between the existing and new rules, a contribution does not include:

- a payment to a trust before 2002 in satisfaction of any amount payable to the trust, or
- the repayment made before 2005, in accordance with terms of repayment established before **[ANNOUNCEMENT DATE + 1]**, to a trust of a loan made by the trust. (This exception is consistent with existing section 5909 of the Income Tax Regulations.)

"contributor"

A "contributor" to a trust is any person or partnership that has made a "contribution" to the trust. See, in this regard, the commentary on the definition "contribution". The definition "contributor" is significant primarily for the purposes of the definitions "resident contributor" and "connected contributor".

Reference should also be made in this context to new paragraphs 94(2)(*k*) to (*o*), under which "look-through" rules are provided to deal with cases where trusts, partnerships or corporations are contributors.

"exempt foreign trust"

An "exempt foreign trust" includes a number of different types of non-resident trusts that are exempt from the application of new subsection 94(3). The expression refers to the following types of non-resident trusts:

- (*a*) a non-resident trust the current income (determined with reference to amended subsection 108(3)) or capital from which can be provided only to one or more physically or mentally infirm dependent individuals, provided that these individuals are non-resident and that any property settled on the trust could reasonably be considered, at the time it was settled, to be necessary for the maintenance of those individuals;

- (*b*) a non-resident trust created after the breakdown of a marriage or common-law partnership of two individuals, the current income (determined with reference to amended subsection 108(3)) or capital from which can be provided only to non-resident children of one of the individuals, if the children are under 21 years of age (or under 31 years of age and enrolled in a specified educational institution) and each "contribution" to the trust (as defined in subsection 94(1)) was to provide for the maintenance of those children;

- (*c*) certain non-resident trusts that could qualify under the definition "total charitable gifts" in subsection 118.1(1) as a recipient permitted for the purposes of the tax credit for charitable gifts;

- (*d*) certain non-resident trusts established exclusively for charitable purposes;

- (*e*) non-resident trusts set up to administer certain types of retirement or pension plans or arrangements;

- (*f*) a non-resident trust that is governed by a "foreign retirement arrangement", as defined in subsection 248(1);

- (*g*) a non-resident trust that is governed by an "employees profit sharing plan", as defined in subsection 248(1);

- (*h*) a non-resident trust that is described in paragraph (*c*) of the definition "exempt trust" in subsection 233.2(1) (i.e., certain foreign unit trusts which are dealt with under the foreign investment entity rules in new sections 94.1 and 94.2); and

- (*i*) a prescribed trust. (Presently, it is not anticipated that any trusts will be prescribed for this purpose.)

"resident beneficiary"

A "resident beneficiary" at a particular time under a trust is a person resident in Canada at the particular time, where:

- at the particular time, there is a "connected contributor" to the trust (as defined in new subsection 94(1)), and

- the person is a beneficiary under the trust and the person's interest in the trust is not solely contingent on the death of a individual who is related at that time to a contributor to the trust (or who would have been related at any earlier time to a contributor to the trust if the individual and every person related at the particular time to the individual had existed at that earlier time).

Under new subsection 94(3), a trust is generally treated as resident in Canada for a particular taxation year if there is a "resident beneficiary" under the trust at the end of the particular year. Under new paragraph 94(3)(*d*), each "resident beneficiary" can be jointly and severally liable with the trust for the trust's income tax liabilities for the particular year under the Act.

"resident contributor"

A "resident contributor" at any time is a person resident in Canada at that time who is a "contributor" to the trust at that time. However, an exemption is provided in this context for new immigrants to Canada (i.e., individuals who have been resident in Canada for a period of, or periods the total of which is, 60 months or less).

Under new subsection 94(3), a trust is generally treated as resident in Canada for a particular taxation year if there is a "resident contributor" to the trust at the end of the particular year. Under new paragraph 94(3)(*d*), a "resident contributor" can be jointly and severally liable with the trust for the trust's income tax liabilities for the particular year under the Act.

ITA
94(2)

New subsection 94(2) of the Act sets out a number of rules for use in applying section 94. These rules are primarily relevant for the purposes of determining whether a transaction constitutes a "contribution" of property to a trust (as defined in subsection 94(1)). These rules are also relevant for the purposes of subsections 94(7) to (9) and the amended reporting rules in subsections 162(10.1) and 163(2.4) and section 233.2. These rules apply to taxation years of trusts that begin after 2000, but in some cases specified below relief is provided with regard to transactions or events that occur before **[ANNOUNCEMENT DATE + 1]**.

Paragraph 94(2)(*a*) deals with transfers or loans (other than a transfer or loan which is an "arm's length transfer" as defined in subsection 94(1)) that may be viewed as indirect transfers or loans of property to trusts, through transfers or loans to other persons or partnerships. A transfer or loan will be considered a direct transfer to a trust where, because of the transfer or loan to another person or partnership,

- the fair market value of one or more properties held by the trust increases, or
- a liability or potential liability of the trust decreases.

Paragraph 94(2)(*b*) deals with cases where a trust holds property the fair market value of which is derived from properties held by another person or partnership. Where this paragraph applies, property transferred or loaned to the other person or partnership is deemed to be transferred to the trust itself. Paragraph 94(2)(*b*) applies where it is reasonable to conclude that one of the reasons for the transfer or loan can reasonably be considered to be connected to the identity of the trust's beneficiaries or other specified persons.

Paragraph 94(2)(*c*) sets out a rule that applies for the purposes of determining the fair market value of property deemed to be transferred to a trust as a consequence of the application of paragraph 94(2)(*a*) or (*b*). This rule is relevant for the purposes of new subsections 94(7) and (8), as well as the penalty provisions for failure to report in subsections 162(10.1) and 163(2.4). The fair market value of the property deemed to have been transferred is considered to be equal to the amount by which the fair market value of the net assets of the trust increased (or the amount by which the liability or potential liability of the trust decreased) due to the transfer or loan that gave rise to the application of paragraph 94(2)(*a*) or (*b*).

Paragraph 94(2)(*d*) applies where property is acquired by a person or partnership as a consequence of the death of an individual. The deceased individual is deemed to have transferred the property to the person or partnership. The paragraph ensures that a person who was resident in Canada immediately before death is generally considered to be a "connected contributor" to the testamentary trust created as a consequence of the person's death. For more detail, see the definitions "connected contributor" and "resident beneficiary".

Paragraph 94(2)(*e*) deems a person or partnership that provides financial assistance to another person or partnership to have transferred property to that other person or partnership. Under paragraph 94(2)(*i*), the fair market value of the property deemed to have been transferred is considered to be equal to the fair market value of the assistance. A deemed transfer will be considered to be a contribution to a trust, by the person or partnership who gives the financial assistance, if the deemed transfer falls within the criteria of the definition "contribution" in subsection 94(1). In this regard, note that the definition contains an exception in respect of arm's length transfers.

Paragraph 94(2)(*f*) applies where services are rendered after **ANNOUNCEMENT DATE** to, for or on behalf of another person or partnership. In these circumstances, the party rendering the service is deemed to have transferred property to the other person or partnership. Paragraph 94(2)(*f*) contains an exception for services rendered in a person's capacity as agent or employee, in which case the paragraph will apply instead to the principal or employer of the agent or employee. Paragraph 94(2)(*f*) also contains an exception for services rendered to a trust that are related to the administration of the trust. Under paragraph 94(2)(*i*), the fair market value of the property deemed to have been transferred is considered to be equal to the fair market value of the services. A deemed transfer under paragraph 94(2)(*f*) will be considered a contribution to a trust, by the person or partnership who rendered the services, if the deemed transfer falls within the criteria of the definition "contribution" in subsection 94(1). In this regard, note that the definition contains an exception in respect of arm's length transfers.

Under paragraph 94(2)(*g*), a corporation is considered to transfer shares that it issues. Similar rules apply to trust and partnership interests, as well as to debt issued by any person or partnership.

Paragraph 94(2)(*g*) applies to shares, debt and interests that are issued after **ANNOUNCEMENT DATE**.

Paragraph 94(2)(*h*) deems a person or partnership that, after **ANNOUNCEMENT DATE**, grants, to another person or partnership, a right to acquire or to be loaned property to have transferred property to that other person or partnership. Under paragraph 94(2)(*i*), the fair market value of the property deemed to have been transferred under paragraph 94(2)(*h*) is considered to be equal to the fair market value of the right.

As noted above, the fair market value of property deemed to have been transferred under paragraphs 94(2)(*e*), (*f*) or (*h*) is determined with reference to paragraph 94(2)(*i*). As is the case with a similar rule in paragraph 94(2)(*c*), paragraph 94(2)(*i*) is relevant for the purposes of new subsections 94(7) and (8), as well as the penalty provisions for failure to report in subsections 162(10.1) and 163(2.4).

Paragraph 94(2)(*j*) is included for greater certainty. It applies where a person or partnership becomes obligated to do an act (e.g., the rendering of a service) that would constitute the transfer of a property to another person or partnership if the act were to occur. Where this is the case, the person or partnership is deemed to become obligated to transfer property to the other person or partnership. This rule is relevant for the purposes of paragraph (*c*) of the definition "contribution" in subsection 94(1).

Paragraph 94(2)(*k*) applies where a particular trust makes a contribution to another trust. Where this is the case, the contribution is deemed to have been made jointly by the particular trust and each person or partnership who is a contributor to the particular trust.

Paragraph 94(2)(*l*) applies where a particular trust makes a contribution to another trust, the contribution is made at the direction (or with the concurrence) of another person and it is reasonable to consider that one of the reasons the contribution is made to the other trust is to enable that other person to avoid liability, as a resident contributor, under paragraph 94(3)(*d*) in respect of the other trust. In such a case, the contribution is deemed to have been made jointly by the particular trust and by that other person.

Paragraph 94(2)(*m*) applies where a partnership makes a contribution to a trust. Where this is the case, partnership members (other than limited partners) are considered to have made a contribution to the trust jointly with the partnership.

Paragraph 94(2)(*n*) applies where a partnership makes a contribution to a trust, the contribution is made at the direction (or with the concurrence) of another person and it is reasonable to consider that one of the reasons the contribution is made to the trust is to enable that other person to avoid liability, as a resident contributor, under paragraph 94(3)(*d*) in respect of the trust. In such a case, the contribution is deemed to have been made jointly by the partnership and by that other person. It should be noted that paragraph 94(2)(*n*) is not relevant to contributions made by a partnership at the direction (or with the concurrence) of a member of a partnership who is not a limited partner, given that paragraph 94(2)(*m*) also applies in this case.

Paragraph 94(2)(*o*) applies where a corporation makes a contribution to a trust, the contribution is made at the direction (or with the concurrence) of another person and it is reasonable to consider that one of the reasons the contribution is made to the trust is to enable that other person to avoid liability, as a resident contributor, under paragraph 94(3)(*d*) in respect of the trust. In such a case, the contribution is deemed to have been made jointly by the corporation and by that other person.

Paragraph 94(2)(*p*) provides that the fair market value of a contribution to a trust at the time it was made is deemed to be the fair market value of the property loaned or transferred that was the subject of the contribution. The rule is useful for the purposes of new subsections 94(7) and (8), as well as the reporting penalty provisions in amended subsections 162(10.1) and 163(2.4). The rule is relevant because a "contribution" is defined as being a transfer or loan, rather than as being the property that was the subject of the transfer or loan.

The examples below illustrate the operation of subsection 94(2) and the definition "contribution" in subsection 94(1).

Example 1

Donald is a long-term resident of Canada. In 2001, Donald pays higher than fair market value consideration for a property acquired from a corporation. A non-resident trust holds shares in the corporation. The fair market value of those shares increases because of the transaction.

Results

1. Under paragraph 94(2)(*a*), Donald is considered to have transferred property to the trust in these circumstances. The exception for "arm's length transfers" is not relevant.

2. As a consequence, Donald is considered to have made a "contribution" to the trust, which results in Donald being a "contributor" and a "resident contributor" to the trust.

Example 2

1. Lucie, who is a long-term resident of Canada, transfers property to Canco on condition that Canco direct Canco's wholly-owned foreign subsidiary (Foreignco-1) to transfer properties to another corporation (Foreignco-2) for consideration that is less than fair market value.

2. Shares of the capital stock of Foreignco-2 are held by a non-resident trust.

3. The fair market value of the Foreignco-2 shares increases as a result of the increase in the fair market value of the property owned by Foreignco-2.

Results

1. The transfers to Canco and to Foreignco-2 are part of the same series of transactions.

2. Because of paragraph 94(2)(*a*), the transfer to Foreignco-2 is considered to be a transfer by Foreignco-1 to the trust. The exception for "arm's length transfers" is not relevant.

3. As a consequence, Lucie is considered to have made a "contribution" to the trust under paragraph (*b*) of the definition "contribution" in subsection 94(1), which results in Lucie being a "contributor" and a "resident contributor" to the trust. Canco is also a "contributor" and a "resident contributor" to the trust.

4. Foreignco-1 is also a "contributor" to the trust, but this does not have any practical consequences because Foreignco-1 is non-resident.

ITA
94(3)

New subsection 94(3) of the Act applies to a non-resident trust (other than an "exempt foreign trust", defined in subsection 94(1)) for a taxation year where, at the end of the year, there is a "resident contributor" to the trust or a "resident beneficiary" under the trust. All of these definitions are explained in detail in the commentary on new subsection 94(1).

Where subsection 94(3) applies to a non-resident trust for a taxation year, the trust is deemed to have been resident in Canada throughout the year for the purposes specified in the subsection. Except to the extent otherwise provided by subsection 94(4), a trust is deemed to be resident in Canada for a taxation year under subsection 94(3):

- for the purposes of applying sections 2 and 115 and computing the trust's income for the year – with the result that the trust is subject to tax under Parts I and I.1 on its world-wide income for the year (Note: These trusts are viewed as resident in Canada for the purposes of tax treaties whether or not they are also considered to be resident in another country. However, subsection 94(3) is structured so that there is no tax arising under the Act for a trust subject to subsection 94(3) in the event that the trust earns only foreign-source income and makes full current distributions of the income to non-resident beneficiaries.);

- for the purpose applying of subsection 94(5) – with the result that, as contemplated by subsection 94(5), the tax consequences under subsection 128.1(4) for a trust that ceases to be resident in Canada apply to the trust (See also the note on paragraph 94(3)(*c*), below.);

- for the purpose of applying clause 53(2)(*h*)(i.1)(*B*) – with the result that the adjusted cost base to a beneficiary of the beneficiary's interest in a trust to which this clause applies is computed in the same way as for interests in trusts resident in Canada;

- for the purpose of applying the definition "non-resident entity" in subsection 94.1(1) – with the result that a beneficiary's interest in the trust is not treated as an interest of a beneficiary in a foreign investment entity for the purposes of new sections 94.1 and 94.2;

- for the purposes of applying subsections 104(13.1) to (29) and 107(5) – with the result that the tax treatment of beneficiaries under the trust accords with the tax treatment available to beneficiaries under trusts that are resident in Canada;

- for the purposes of applying sections 233.3 and 233.4 – with the result that the trust is required to file information returns under sections 233.3 (information return on a foreign property holdings that cost in excess of $100,000) and 233.4 (information return on foreign affiliates);

- for the purpose of determining the liability of the trust for tax under Part XIII - with the result that the trust is exempt from Part XIII tax on amounts paid or credited to it; and

- for the purpose of determining the rights and obligations of the trust under sections 150 to 180 – with the result that various administrative provisions in the Act apply in the same way as to other trusts resident in Canada. These provisions include those with regard to the filing of returns, assessments, tax payments, arrears interest, refund interest, instalment interest, penalties, refunds and appeals.

Paragraph 94(3)(*b*) provides that a trust that is subject to subsection 94(3) is entitled to claim foreign tax credits against its Canadian income tax in accordance with the rules in section 126, except with regard to any taxable income earned in Canada (as would otherwise be determined under subsection 115(1)).

Paragraph 94(3)(*c*) clarifies that a non-resident trust that becomes subject to subsection 94(3) for a particular taxation year, after not being subject to either it or existing paragraph 94(1)(*c*) for the preceding year, is deemed to become resident in Canada at the beginning of the particular year. As a result, the cost amount of each of the properties (other than taxable Canadian properties) held by the trust at the beginning of the particular year is deemed by subsection 128.1(1) to be the fair market value of the property at the beginning of the particular year. Note, in this regard, that paragraph 94(3)(*c*) complements the rule in subsection 94(6) in the case where a non-resident trust ceases to be an "exempt foreign trust" (as defined in subsection 94(1)). In this case, subsection 94(6) establishes the beginning of a new "stub" taxation year to which subsection 94(3) may apply. If subsection 94(3) does apply for that "stub" year, subsection 128.1(1) would apply with regard to the properties (other than taxable Canadian properties) held by the trust at the beginning of that "stub" year.

Paragraph 94(3)(*d*) imposes liabilities for a taxation year on persons who, at the end of the year, are "resident contributors" or "resident beneficiaries". Where subsection 94(3) applies to a trust for a taxation year, each of these persons is jointly and severally liable with the trust in respect of the trust's obligations under sections 150 to 180, including its Part I.1 obligations that arise as a consequence of subsection 180.1(4). Typically, the most significant obligation in this context is the obligation to pay tax instalments pursuant to section 156. However, the extent of the joint liability imposed by paragraph 94(3)(*d*) is limited by new subsection 94(7) – which is explained in the commentary below.

Note, in particular, that subsection 94(3) does not result in the creation of any obligations for a trust that is subject to subsection 94(3) to withhold tax on distributions to non-resident beneficiaries under Part XIII or to pay any tax under Part XII.2. As noted above, one of the effects of subsection 94(3) is that the trust is not liable in connection with distributions of Canadian-source income to the non-resident trust. However, the rules in new subsection 104(7.01) are designed so that there will be a reasonable level of Part I tax in respect of Canadian-source income received by the trust in the event the trust also distributes income to non-resident beneficiaries.

ITA
94(4)

New subsection 94(4) of the Act provides that the rules in subsection 94(3) treating non-resident trusts as resident in Canada do not apply for certain limited purposes:

- the definition "exempt foreign trust" – thus ensuring that there is no circularity due to fact that the definition "exempt foreign trust" is used in subsection 94(3);

- computing income or loss from property, or any taxable capital gain or allowable capital loss, because of the application of subsection 75(2) – thus providing that income generated from a property transferred by a non-resident trust to a reversionary trust is not attributed back if the non-resident trust is deemed to be resident in Canada under subsection 94(3);

- proposed paragraph 107.4(1)(*c*), other than subparagraph 107.4(1)(*c*)(*i*), and proposed subparagraph (*f*)(ii) of the definition "disposition" in subsection 248(1)[6] – thus ensuring that proposed rules allowing in some cases for a rollover of property on transfers involving no change in beneficial ownership generally do not apply to transfers to a trust deemed to be resident in Canada by subsection 94(3); and

- paragraph (*a*) of the definition "mutual fund trust" in subsection 132(6) – a reference which makes it clear that a trust deemed to be resident in Canada by subsection 94(3) will not be treated as a mutual fund trust for any purpose.

Furthermore, except as otherwise permitted in writing by the Minister of National Revenue, subsection 94(3) does not relieve a payer of Canadian-source income the obligation to withhold under section 215 in connection with amounts received by a trust deemed to be resident of Canada by subsection 94(3). This is so even though such a trust is not liable for Part XIII tax on amounts paid or credited to it, because of the application of subparagraph 94(3)(*a*)(iii). The trust would be expected to apply for a refund of such tax, which would be given unless there are any outstanding liabilities of the trust with regard to Part I tax.

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[6] The measures were contained in a detailed Notice of Ways and Means Motion tabled on June 5, 2000.

ITA
94(5)

New subsection 94(5) of the Act applies to a trust with regard to a particular period that (without reference to the combined application of subsections 94(5) and 128.1(4)) would be a taxation year of the trust that immediately follows a taxation year of the trust throughout which it is resident in Canada because of the application of subsection 94(3). If the trust is not resident in Canada at the end of the particular period (i.e., because the criteria in subsection 94(3) for deeming the trust to be resident in Canada are no longer satisfied), the trust is deemed to have ceased to reside in Canada at the earliest time in the particular period at which there is neither a "resident contributor" to the trust nor a "resident beneficiary" under the trust. These two definitions are explained in the commentary on subsection 94(1).

In such circumstances, the cessation of residence in Canada results in the application of paragraph 128.1(4)(*a*). As a consequence of that paragraph, a taxation year of the trust is considered to have ended immediately before the earliest time in the particular period described above. At the end of that taxation year, the criteria in subsection 94(3) are satisfied. Accordingly, the trust would be subject to tax under Parts I and I.1 on its world-wide income for that year because it is considered to be resident in Canada under subsection 94(3).

ITA
94(6)

New subsection 94(6) of the Act generally provides that, if a trust becomes or ceases to be an exempt foreign trust at any time, the trust's taxation year is deemed to have ended immediately before that time, a new "stub" taxation year is deemed to have begun at that time and the trust is deemed not to have established a fiscal period before that time. However, subsection 94(6) does not apply where a trust ceases to be an exempt foreign trust because it becomes resident in Canada.

Subsection 94(3) may apply in respect of the later "stub" taxation year of the trust if the criteria set out in that subsection are satisfied at the end of that year. Where this is the case, the trust would be subject to tax under Parts I and I.1 on its world-wide income for that later "stub" year because it would be considered under subsection 94(3) to be resident in Canada for that year.

ITA
94(7) to (9)

New subsection 94(7) of the Act allows for a limitation of the amount that may be recovered from a person who would otherwise be jointly and severally liable for the entire amount of the trust's tax obligations under the Act. Subsection 94(7) applies to a person in respect of a particular taxation year of a trust where three conditions are satisfied.

The first condition is that the person must have filed on a timely basis all information returns required to be filed by the person in respect of the trust under section 233.2 (or within such later period as is acceptable to the Minister of National Revenue).[7] However, the first condition need not be satisfied if the second condition (below) is satisfied because of the $10,000 contribution test referred to below.

The second condition is satisfied in respect of a particular taxation year of the trust:

- where the person is jointly and severally liable with the trust only because the person was a "resident beneficiary" under the trust at the end of the particular year,[8] or

- where, at the end of the particular year, the total fair market value (determined with reference to paragraphs 94(2)(*c*), (*i*) and (*p*) and subsection 94(9)) of contributions made to the trust by the person (or another person not dealing at arm's length with the person) is not more than the greater of $10,000 and 10% of the total fair market value of all contributions to the trust.[9]

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[7] Paragraph 94(7)(*a*).

[8] Subparagraph 94(7)(*b*)(i).

[9] Subparagraph 94(7)(*b*)(ii).

The third condition is satisfied in respect of a person and a particular taxation year of the trust where it is reasonable to conclude that each transaction or event that occurred before the end of the particular year at the direction of, or with the concurrence of, the person satisfied the following conditions:

- none of the purposes of the transaction or event was to enable the person to minimize liability under paragraph 94(3)(*d*) in respect of the trust,[10] and

- the transaction or event was not part of a series of transactions or events any of the purposes of which was to enable the person to minimize liability under paragraph 94(3)(*d*) in respect of the trust.[11]

There are a number of transactions or events, or series of transactions or events, which may result in a failure to satisfy the third condition. For example, an artificial dilution of a person's relative contribution in the trust (i.e., below the 10% level) could well be impugned. Likewise, corporate distributions that have the effect of minimizing the impact of the three-year rule described in subsection 94(9) could also be offensive for these purposes.

Reference should be made in this context to the definition "contribution" in subsection 94(1), as well as to related rules in subsection 94(2).

Where subsection 94(7) applies to a person in respect of a taxation year of a trust, the amount recoverable at any time from the person in respect of the year is limited to the person's "recovery limit" in respect of the trust and the year. Under subsection 94(8), the amount of the recovery limit at any time is calculated as follows:

- ADD amounts payable and amounts previously paid by the trust to the person in respect of the person's beneficial interest in the trust;

- ADD previous proceeds from the disposition of the person's interest in the trust, not otherwise taken into account above;

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[10] Subparagraph 94(7)(*c*)(i).

[11] Subparagraph 94(7)(*c*)(ii).

- ADD the fair market value of benefits conferred by the trust on the person, not otherwise taken into account above;

- ADD the total fair market value (determined with reference to paragraphs 94(2)(*c*), (*i*) and (*p*) and subsection 94(9)) of contributions made to the trust by the person, to the extent that this amount exceeds the total of the first three amounts; and

- SUBTRACT previous recoveries by the CCRA under subsection 94(3) from the person in respect of the trust and the year or a preceding taxation year of the trust.

As indicated above, subsection 94(9) affects the calculation of the fair market value of a "contribution" to a trust. It applies where the contributed property is a share, a right to acquire a share, or other property primarily deriving its value from a share or a right to acquire a share.

For the purpose of determining whether the "recovery limit" limitation applies to a contributor to a trust in respect of a transfer to the trust and of determining the amount of the "recovery limit", the fair market value of contributed property is deemed by subsection 94(9) to be the greater of:

- its fair market value, otherwise determined, at the time it was transferred (see in this regard paragraph 94(2)(*p*)); and

- its fair market value (or the fair market value of substituted property) at the end of the third calendar year ending after its transfer to the trust.

Subsection 94(9) is intended to allow for a reasonable opportunity for recovery of tax by the CCRA in the context of a series of transactions involving the transfer of shares or similar property. For example, an estate freeze might occur under which common shares with a nominal initial fair market value are transferred directly or indirectly to a non-resident trust. In these circumstances, it would be inappropriate to limit a recovery of tax to the initial fair market value of the shares.

Clause 11

ITA
94.1

Existing section 94.1 of the Act applies where a taxpayer has invested in an offshore investment fund and one of the main reasons for the investment is to reduce or defer the tax liability that would have applied to the income generated from the underlying assets of the fund if such income had been earned directly by the taxpayer. In these circumstances, existing section 94.1 generally requires an amount to be included in computing the taxpayer's income from the investment. This amount is determined, in general terms, by multiplying the cost amount of the taxpayer's investment by a factor based on interest rates prescribed under Part XLIII of the Regulations.

Section 94.1 is replaced by provisions in new sections 94.1 to 94.3, which contain rules governing the tax treatment of interests in foreign investment entities (FIEs). Under the new rules, a taxpayer's investment motives are no longer relevant. In computing a taxpayer's income for a taxation year, where a taxpayer so elects and has sufficient information to comply, new section 94.1 generally requires the inclusion of the taxpayer's share of FIE income for each FIE taxation year that ends in the taxpayer's taxation year. New section 94.2 applies in place of the rules in section 94.1 in all other cases. Under section 94.2, a taxpayer takes into account the annual increase or decrease in the fair market value of the taxpayer's interest in an FIE in computing the taxpayer's income from the FIE. Section 94.3 is designed to prevent double taxation with respect to amounts included in income under sections 94.1 and 94.2.

New section 94.1 applies to taxation years of Canadian investors that begin after 2000.

The table below provides an overview of new sections 94.1 to 94.3 and related provisions.

Issue	Summary	References
1. Which taxpayers are subject to the new FIE rules?	A. All taxpayers, except exempt taxpayers. Except as indicated in (C), below, FIE rules do not apply to non-resident taxpayers.	S.94.1(2) to (4) and 94.2(3) and (4). "Exempt taxpayer" (s.94.1(1)). Non-resident taxpayers: see also s.94.1(3) and 94.2(5).
	B. Partnerships with members resident in Canada must allocate FIE income to those members.	Existing section 96, including exception in s.96(1.9). See also s. 94.2(6) for application to cases where partnership members become resident in Canada.
	C. Controlled foreign affiliates.	New s. 95(2)(g.2).
2. What property is subject to the new FIE rules?	A. Participating interests (other than exempt interests) in foreign investment entities. However, if no taxation year of an FIE has ended before the end of the taxpayer's taxation year, the FIE rules do not apply to the taxpayer for the taxpayer's year in respect of the FIE.	S.94.1(2). The following definitions in s.94.1(1): "entity", "non-resident entity", "foreign investment entity", "exempt interest" and "participating interest".
	B. Where property described in (A) is a right to acquire property or is not capital property, it is not subject to section 94.1 but it is subject to s.94.2.	S. 94.1(4) and 94.2(3).
	C. Interests in non-resident entities, where those interests track returns in respect of investment property. This property is subject only to s.94.2, not to s.94.1.	S. 94.2(9). See also amended s.91(1).
	D. Interests in certain foreign insurance policies. This property is subject only to s.94.2, not s.94.1.	S. 94.2(10).

Issue	Summary	References
3. What is the difference in the tax treatment of FIE interests between s.94.1 and s.94.2?	A. Section 94.1. Taxes only investor's "share" of FIE's income (e.g., does not include FIE's share of unrealized gains).	S.94.1(3).
	B. Section 94.2. Full appreciation/decline in fair market value recognized on an annual basis.	S. 94.2(4)
4. How will foreign affiliates of taxpayers resident in Canada be treated under new FIE rules?	Subject to s. 94.2(9) (tracked interests), a taxpayer's share of the capital stock of a controlled foreign affiliate is exempt from the new FIE rules. In certain cases, a taxpayer can elect to have a foreign affiliate treated as a controlled foreign affiliate.	Paragraph (*a*) of the definition "exempt interest". S. 94.1(12).
5. If a non-resident corporation that is an FIE pays out dividends, how are these dividends taxed?	A. General principle: existing rules apply.	Existing s. 90 and 113.
	B. Relief provided to prevent double taxation. This relief extends to taxable distribution from other FIEs (e.g., trusts).	S. 94.3.
	C. Special rules in the event that the dividends paid to another FIE.	S. 94.1(5)A(*g*).

Issue	**Summary**	**References**
6. In what circumstances is a taxpayer subject to sections 94.1 and 94.2, respectively?	A. S.94.2 rule applies, except as expressly provided otherwise.	S. 94.1(2) to (4) and s. 94.1 (3).
	B. Election to use s.94.1 available.	S. 94.1(4)
	C. Requirement to use s.94.2 where insufficient information to use s.94.1.	S. 94.1(17)
	D. Requirement for FIEs to calculate own income with reference to s.94.2.	S. 94.1(4)(*e*)
	E. Requirement to use s. 94.2 in the case of properties described in 2(B), (C) and (D), above.	See references in 2(B), (C) and (D).

The table above reflects two main variations from the outline of the proposals put forward for consultation for foreign investment funds in the 1999 budget papers and the November 30, 1999 press release issued by the Minister of Finance. First, in recognition of the complexity associated with proposed section 94.1 and the likelihood that most investors will not have sufficient information to comply with the section, the simpler mark-to-market regime has been made the "default" regime. Second, there is no exemption provided for foreign investment funds that distribute their income annually for the following reasons:

- these distributions may not necessarily be subject to immediate Canadian income tax;

- such an exemption could inappropriately allow for the use of tiered structures under which a fund that distributes annually itself invests, directly or indirectly, in a foreign investment fund that does not distribute annually; and

- to provide equality of treatment between domestic and foreign investment funds, it would be necessary to use income for Canadian tax purposes for the purpose of such an exemption.

However, income of this nature is not generally calculated by foreign investment funds and would not normally be known by investors.

ITA
94.1(1)

New subsection 94.1(1) of the Act defines a number of expressions for the purpose of section 94.1. These definitions are also relevant for the purposes of sections 94.2 and 94.3.

"carrying value"

The "carrying value" of a property held by an entity at any time is the amount at which the property is valued as of that time for the purpose of the entity's balance sheet, except where

- the balance sheet was not prepared in accordance with accounting principles similar to generally accepted accounting principles used in Canada, or
- the balance sheet was not distributed within 3 months after that time.

The carrying value of a property is generally expected to be either the historical cost of the property or the fair market value of the property. In the event that a qualifying balance sheet is not prepared or distributed on a timely basis or the property is not expressly valued, a property's carrying value is the amount at which the property would have been valued using generally accepted accounting principles used in Canada.

The carrying value of property is relevant primarily for the purpose of determining whether a non-resident entity is an FIE. This determination is made at the end of the entity's taxation year. (For further detail, see the commentary on the definition "foreign investment entity".) However, it should be noted that the look-through rule in subsection 94.1(10) can affect the properties considered to be owned by an entity and the carrying values of the entity's properties. This look-through rule applies where the entity has a "significant interest" (defined in subsection 94.1(11)) in a corporation, partnership, or trust. For the purposes of the look-through rule, the time at which the determination of carrying value is made is the end of the taxation year of the first tier non-resident entity (whether or not lower tier entities share the same taxation year).

"entity"

An entity includes a trust, a corporation, an organization and a fund. Subject to the comments below, it does not include a partnership. The new rules are designed so that, in the case of partnerships, members' shares of incomes and losses are allocated in accordance with section 96 (including new subsection 96(1.9), described in the commentary below).

An "entity" does, however, include a partnership to the extent that this intent is evident in section 94.1. The intent is evident in the definition "carrying value" and paragraph 94.1(10)(*c*), as it may be necessary to determine the carrying value of the assets of a partnership because of the operation of subsection 94.1(10).

"excluded investment business"

An "excluded investment business" is a type of "investment business" (as described in the commentary below) that is provided favourable tax treatment. The favourable treatment arises because of the reference to "excluded investment business" in the definition "qualifying corporation". A publicly traded share issued by a "qualifying corporation" is generally an "exempt interest" to which the FIE regime in sections 94.1 and 94.2 does not apply. In addition, there is a reference to an "excluded investment business" in subsection 94.1(12) which permits an election to be made by a taxpayer to treat a foreign affiliate principally carrying on an excluded investment business as a controlled foreign affiliate of the taxpayer.

In general terms, an "excluded investment business" is a business of a corporation in which it finances the operations of related corporations that do not carry on investment businesses. Thus, an "excluded investment business" has a substantial link to active businesses (or, more precisely, to businesses that are not investment businesses).

More specifically, an "excluded investment business" of a particular corporation in a period is defined as an "investment business" of the particular corporation in the period where, throughout the part of the period throughout which the business was carried on, all or substantially all of the particular corporation's assets used or held in the business are participating interests or debt issued by one or more corporations:

- related to the particular corporation (or in which the particular corporation has a "significant interest", as defined in subsection 94.1(11)), and

- the principal businesses of which are not investment businesses.

"exempt interest"

An "exempt interest" of a taxpayer in an FIE is each of the following properties:

- a participating interest held by the taxpayer in a controlled foreign affiliate of the taxpayer (including an affiliate that is a controlled foreign affiliate because of an election under new subsection 94.1(12)),

- as described in greater detail below, certain shares and options in respect of publicly traded corporations,

- where the taxpayer is a financial institution (as defined in subsection 142.2(1)), a participating interest held by the taxpayer that is mark-to-market property (as defined in that same subsection), and

- a participating interest in a testamentary trust, provided the interest has not been acquired for consideration.

The rules in sections 94.1 and 94.2 generally do not apply in respect of "exempt interests". In most cases, the time of determination for whether a property is an "exempt interest" in an entity is the end of a taxation year of the entity. See, in this regard, subsection 94.1(2).

As noted above, an exempt interest includes certain shares and options with respect to publicly traded FIEs. Given the definition "foreign investment entity", most non-resident financial institutions and real estate development companies, and some resource companies, are expected to be classified as FIEs. Consequently, shares issued by these entities (as well as options in respect of these shares) would be subject to the rules in section 94.1 or 94.2 if it were not for the definition "exempt interest". Under paragraph (*b*) of the definition "exempt interest", the FIE rules will not apply to a taxpayer's shares and rights to acquire shares of a class of the capital stock of a non-resident corporation held during a taxation year of the taxpayer where, in the period in the year during which the property was held:

- the class is widely held, actively traded and listed on a prescribed stock exchange (note: stock exchanges listed in section 3200 or 3201 of the Regulations are to be prescribed for this purpose), and
- either
    - the corporation's principal business was not an investment business (as defined in subsection 94.1(1) and described in the commentary below) in the period, or
    - the corporation is a qualifying corporation in the period. (See commentary below on the definition "qualifying corporation".)

"exempt taxpayer"

An individual is an "exempt taxpayer" for a taxation year where the individual, before the end of the year, was a resident of Canada for a period of, or periods the total of which is, 60 months or less. (Children who have always been resident in Canada cannot fall within the 60-month exception.)

The rules in new sections 94.1 and 94.2 do not apply in respect of periods during which a taxpayer qualifies as an exempt taxpayer, due to the reference to exempt taxpayers in paragraph 94.1(2)(*a*) and subsections 94.2(9) and (10). The 60-month exemption for new immigrants to Canada is similar to an exemption in the rules for non-resident trusts in existing section 94.

Tax-exempt entities to which subsection 149(1) applies are also included as exempt taxpayers. However, this inclusion does not apply to retirement compensation arrangements and qualifying environmental trusts for which alternative income tax rules are provided under Parts XI.3 and XII.4. The inclusion also does not apply to insurers to which paragraph 149(1)(*t*) applies, given the taxability of those insurers pursuant to subsection 149(4.1).

The express reference to tax-exempt entities is generally of significance for the purposes of calculating Part I tax only in the context of the narrow circumstances to which new subsection 94.2(16) applies. That subsection contemplates a case where a taxpayer ceases to be an "exempt taxpayer" and subsequently becomes an "exempt taxpayer". However, the reference to tax-exempt entities may also be of significance in the context of Part XI (foreign property limits), given that the application of sections 94.1 and 94.2 has an impact on the cost amount of participating interests in FIEs.

"foreign bank"

The definition "foreign bank" has the same meaning as in subsection 95(1). The expression is used in the definition "investment business".

"foreign investment entity"

The new tax regime for FIEs in sections 94.1 and 94.2 generally applies only to participating interests in a foreign entity that is a "foreign investment entity".

A non-resident entity is generally a "foreign investment entity" throughout one of its taxation years where the total carrying value of its investment property is greater than 50% of the total carrying value of all of its property at the end of the year. In making this determination, the entity's property must be identified as either investment property or other property and it must be assigned a carrying value.

A foreign investment entity does not, however, include:

- an "exempt foreign trust" under subsection 94(1) (other than a widely-held mutual fund trust referred to in paragraph (*c*) of the definition "exempt trust" in existing subsection 233.2(1)), or

- a discretionary personal trust (or, more precisely, a trust that is not a "non-discretionary trust").

For more detail, see the commentary on the expressions "entity", "non-resident entity", "investment property" and "carrying value" in subsection 94.1(1). "Non-discretionary trust" is newly defined in subsection 248(1), with reference to the definition of the same expression in subsection 17(15).

Special rules in subsections 94.1(10) and (13) generally limit the circumstances in which a non-resident entity falls within the definition "foreign investment entity".

"investment business"

The expression "investment business" is used in the definitions "exempt interest" and "investment property", as well as in subsection 94.1(12) (election to be a controlled foreign affiliate). The definition "investment business" is similar to the definition of the same expression in existing subsection 95(1). Note, however, that in this definition:

- there is no exception for traders and dealers in securities or for the lending of money, the leasing or licensing of property or the insurance or reinsurance of risks;

- there is a greater accommodation of real estate businesses and businesses involved in the development of foreign resource properties;

- there is no explicit requirement for a specific number of full-time employees for the exceptions to the definition to apply; and

- the supporting definitions and rules contained in subsections 95(1) to (2.4) are not relevant.

"investment property"

The expression "investment property" includes a list of specified properties. Most of the specified properties (e.g., shares, partnership interests, real estate and resource properties) are also specified in the definition of the same expression in subsection 95(1). In addition to the properties also specified in the definition in subsection 95(1), "investment property" held by a particular entity includes:

- an interest in an organization, fund or other entity;
- most derivative financial products; and
- interests, options and rights in respect of the above properties.

It should be noted, however, that "investment property" in subsection 94.1(1) does not include accounts receivable that arise from the sale of tangible property or services in the ordinary course of a business (other than an "investment business", described above).

The definition is primarily relevant for purposes of the determining whether a non-resident entity is a "foreign investment entity".

"non-resident entity"

One of the requirements for an entity to be an FIE to which sections 94.1 and 94.2 apply is that the entity must be a "non-resident entity".

In addition to non-resident corporations and trusts, a "non-resident entity" includes any other type of entity

- organized under the laws of a jurisdiction outside Canada, or
- the governance of which is provided under the laws of a jurisdiction outside Canada.

"participating interest"

A "participating interest" in an entity means a share of the capital stock of, or an interest in, the entity. It also includes a right to acquire such a share or interest. Section 94.1 or 94.2 generally applies to a taxpayer in respect of a participating interest in an FIE that is not an "exempt interest" of the taxpayer.

"qualifying corporation"

Shares issued by a qualifying corporation are generally exempt from the FIE regime in sections 94.1 and 94.2 because of the definition "exempt interest" (described in the commentary above), provided the shares are widely-held, actively traded and listed on a prescribed stock exchange.

In general terms, a "qualifying corporation" is a corporation that (directly or indirectly) finances the active business operations of related corporations.

More specifically, a "qualifying corporation" in a period is defined as a particular corporation all or substantially all of the assets of which are, throughout the period, any combination of:

- properties (other than investment properties), and
- shares or debt issued by one or more other corporations each of which
    - is, at any time in the period, a corporation all of the shares of which (other than directors' qualifying shares) are held by any combination of the particular corporation and related corporations, and
    - either
        - has as its principal business an excluded investment business or a business (other than an investment business), or
        - is itself a qualifying corporation in the period.

Reference should also be made to the commentary on the definition "excluded investment business".

"taxation year"

The "taxation year" of a non-resident entity is a calendar year. However, if the entity is a corporation, its taxation year is the period, not exceeding 53 weeks, for which its accounts are ordinarily made up.

ITA
94.1(2) to (4)

New subsection 94.1(2) of the Act sets out the common conditions for the application of the FIE rules in section 94.1(3) (accrual regime) and 94.2(4) (mark-to-market regime). For the accrual or mark-to-market regimes to apply to a taxpayer for a particular taxation year in respect of a participating interest held in the particular year by the taxpayer in a non-resident entity, all of the following conditions set out in subsection 94.1(2) must be satisfied:

- the taxpayer is not an "exempt taxpayer" for the particular year;[12]

- a taxation year of the entity ended at or before the end of the particular year and, at the end of the latest such taxation year of the entity, the entity was an FIE;[13]

- where the interest or identical property to the interest was held by the taxpayer at the end of the latest such year, the interest or the identical property was not an "exempt interest" in respect of the taxpayer;[14] and

- where neither the interest nor identical property to the interest were held by the taxpayer at the end of the latest such year, the interest and each identical property was not an exempt interest while held in the particular year by the taxpayer.[15]

Notwithstanding the above, the mark-to-market regime, rather than the accrual regime, applies where the exceptions under subsection 94.1(4) apply. Subsection 94.1(4) provides that the accrual regime applies only to capital property and only where an election to use the accrual regime has been made at the earliest opportunity. Moreover, the accrual regime does not apply to a taxpayer for a taxation year in respect of a participating interest in a non-resident entity in the following cases:

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[12] Paragraph 94.12(2)(*a*).

[13] Paragraphs 94.1(2)(*b*) and (*c*).

[14] Paragraph 94.1(2)(*d*).

[15] Paragraph 94.1(2)(*e*).

- where section 94.1 does not apply because of the operation of subsection 94.1(17) (insufficient information),

- where, because of subsection 94.2(9) (tracked interests), subsection 94.2(3) applies or has applied to the taxpayer in respect of the interest or identical property,

- where the taxpayer is itself an FIE,[16] or

- where the interest is an option or similar right to acquire.

Where the accrual regime does apply to a taxpayer for a particular taxation year in connection with one or more of a taxpayer's identical participating interests in a non-resident entity, subsection 94.1(3) provides:

- The taxpayer's "income allocation" in respect of those interests for a taxation year of the entity ending in the particular year is added in computing the amount included in the taxpayer's income under subsection 94.1(3), to the extent that the taxpayer held those interests at the end of the entity's year. (However, in order to clarify the application of section 114 to part-year residents and to ensure that section 94.1 does not affect the taxability of non-resident taxpayers, subsection 94.1(3) does not apply to a taxpayer for a taxation year in respect of an FIE's taxation year that ends in the taxpayer's year where the taxpayer is not resident in Canada at the end of the FIE's year.)

- The taxpayer's "loss allocation" in respect of those participating interests is deductible to the extent that there has previously been a net cumulative positive balance determined under subsection 94.1(3) in respect of the taxpayer for such property in respect of preceding taxation years of the entity. An unused loss allocation is carried forward to offset the total amount otherwise required to be computing the taxpayer's income under subsection 94.1(3) in respect of identical participating interests for a subsequent taxation year of the entity.

- A taxpayer's specified tax allocation in respect of the entity's year is treated in the same way as a loss allocation. However, unlike a

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[16] See commentary on paragraph 94.1(5)A(*a*) for more detail.

> loss allocation, a specified tax allocation can arise for the same entity's year as an income allocation. Where this is the case, the specified tax allocation can directly offset the income allocation. A taxpayer's specified tax allocation, as determined under subsection 94.1(8), represents the taxpayer's grossed-up share or income of profits tax paid by the entity in the year on account of a liability for income or profits tax for the entity's year or an earlier year of the entity. The taxpayer's share of taxes in respect of the liability year is determined with reference to the taxpayer's position in the entity at the end of the liability year.

The examples after the commentary on subsections 94.1(5) and (6) illustrate the operation of subsection 94.1(3).

ITA
94.1(5) and (6)

New subsection 94.1(5) of the Act provides for the calculation of a taxpayer's income allocation in respect of participating interests in an FIE. A taxpayer's income allocation in respect of one or more identical participating interest in an FIE held by the taxpayer at the end of the FIE's taxation year is included in computing the taxpayer's income under subsection 94.1(3). In general terms, a taxpayer's income allocation in respect of participating interests in an FIE is the proportion of the FIE's income for a taxation year that the fair market value of those interests is of the fair market value of all participating interests in the FIE.

The calculation of a taxpayer's income allocation in respect of an FIE depends on a calculation of income for the FIE in accordance with rules set out in paragraphs 94.1(5)A(*a*) to (*i*). The calculation for a particular taxpayer generally only takes into account an FIE's taxation years that end after the particular taxpayer first holds a participating interest in the FIE in a taxation year of the taxpayer that begins after 2000. The first such FIE taxation year in respect of a taxpayer is defined in subsection 94.1(6) as the "fresh start year" of the FIE in respect of the taxpayer. This permits taxpayers to make independent calculations of an FIE's income for the purpose of determining income allocations under section 94.1.

The special rules that apply in calculating an FIE's income in respect of an investor taxpayer for the FIE's fresh start year and subsequent years are as follows:

- Subject to three exceptions, the FIE is generally treated as having been a taxpayer resident of Canada throughout its existence.[17] First, this rule does not apply for the purposes of proposed subsection 107.4(1) or proposed paragraph (*f*) of the definition "disposition" in subsection 248(1),[18] with the result that property that is transferred to the FIE without there being any change in the beneficial ownership of the property is considered to have been transferred to the FIE under subsection 69(1) at the fair market value of the property. Second, this rule does not apply for the purposes of section 91 with the result that the FIE will not itself be required to include an amount in respect of foreign accrual property income in computing the FIE's income. Third, this rule does not apply for the purposes of paragraph 94.1(4)(*e*) with the result that section 94.2 (rather that section 94.1) potentially applies in the event that the FIE owns a participating interest in another FIE.

- Each property held by the FIE at the beginning of the fresh start year is deemed to have been disposed of for its fair market value immediately before that time and reacquired for the same amount at that time.[19]

- Each discretionary deduction permitted in computing the FIE's income for the FIE's fresh start year and subsequent taxation years is deemed to have been claimed to the extent designated by the investor taxpayer. Thus, in calculating an income allocation in respect of the FIE, the investor taxpayer will be permitted to claim deductions such as capital cost allowance.[20]

- The FIE is assumed to have deducted the greatest amounts permissible, for its taxation year preceding the fresh start year, under sections 20, 138 and 140.[21] These amounts are added in computing the FIE's income for the fresh start year, but appropriate deductions under these sections can be claimed for the fresh start year and subsequent taxation years. In the context of the reserve for life insurers under subsection 138(3), it is intended to amend paragraph (*c*) of the definition "reported reserve" in subsection 1408(1) of the Regulations so that the FIE can have a "reported reserve".

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[17] Paragraph 94.1(5)A(*a*).

[18] Proposed section 107.4 and a new definition "disposition" in subsection 248(1) are contained in a detailed Notice of Ways and Means Motion tabled on June 5, 2000 .

[19] Paragraph 94.1(5)A(*b*). Compare paragraph 149(10)(*b*)

[20] Paragraph 94.1(5)A(*c*).

- The FIE is deemed not to have been in existence before the fresh start year for the purposes of sections 37, 65 to 66.4 and 66.7.[22] As a consequence, the scientific research and resource expenditure pools to which these sections refer are ignored, to the extent that these pools were generated before the fresh start year.

- The FIE is not permitted to deduct any amount under subsection 20(11) or (12) in respect of its foreign tax.[23] However, foreign tax will be taken into account because the FIE's specified tax allocation (as determined under new subsection 94.1(8)) can offset amounts otherwise included in income under subsection 94.1(3).

- If the FIE is a trust, no amount is considered deductible under subsection 104(6) in determining its income for the year.[24] Double taxation for the investor taxpayer is avoided through the application of new subsection 94.3(2). In addition, no deemed disposition day under subsection 104(4) is determined in respect of the trust, whether or not the FIE falls outside the restricted meaning of "trust" for this purpose under subsection 108(1).

- If the investor taxpayer is a corporation resident in Canada and the FIE is a foreign affiliate of the taxpayer, any dividends received by the FIE from a foreign affiliate of the taxpayer in respect of which the taxpayer has a qualifying interest (as determined under paragraph 95(2)(*m*)) are not included in the FIE's income.[25] Note, that this rule does not apply in the event that the FIE's

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21. Paragraph 94.1(5)A(*d*). Compare paragraph 149(10)(*a*.1).
22. Paragraph 94.1(5)A(*e*). Compare paragraph 149(10)(*c*).
23. Paragraph 94.1(5)A(*f*).
24. Paragraph 94.1(5)A(*f*).
25. Paragraph 94.1(5)A(*g*).

interest in the foreign affiliate is subject to the mark-to-market regime in subsection 94.2(4). However, an income inclusion resulting from the application of subsection 94.2(4) for the FIE in some cases can, however, be offset by the deduction provided under new subsection 94.3(2).

- Where the FIE has an interest in another FIE, there is no "deferral amount" taken into account in computing the FIE's income pursuant to new subsection 94.2(4).[26] (The fresh start rule described above eliminates the need for a "deferral amount".)

- Participating interests in controlled foreign affiliates of the investor taxpayer (rather than controlled foreign affiliates of the FIE) are treated as "exempt interests" of the FIE.[27]

A taxpayer's income allocation in respect of a participating interest in a FIE is the proportion of an entity's income for a taxation year (determined in accordance with the special rules detailed above) that the fair market value at the end of the year of the participating interest is of the fair market value at that time of all participating interests in the entity (other than rights to acquire shares of the capital stock of, or to acquire interests in, the entity).

For further details, see the related commentary on the expressions "foreign investment entity", "exempt interest" in subsection 94.1(1), as well as the commentary on subsection 94.1(5) (income allocation), subsection 94.1(7) (loss allocation) and subsection 94.1(8) (specified tax allocation).

The examples below illustrate the operation of subsections 94.1(3) and (5). It should be noted in this context that any negative amount otherwise resulting from the formula in paragraph 94.1(3)(*a*) is deemed to be nil as a result of the application of section 257.

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[26] Paragraph 94.1(5)A(*h*).

[27] Paragraph 94.1(5)A(*i*).

Example 1

Canco owns shares in the capital stock of FIE-1, which like Canco has a calendar taxation year. Canco's income (loss) allocations for 2001, 2002, 2003, 2004 and 2005 are (100), 25, 90, (20) and 50, respectively.

Results

1. The amount included under subsection 94.1(3) in Canco's income for 2001 is nil (B = 100). The amount determined under subparagraph 94.1(3)(*b*)(i) for 2001 is 100, which can be carried forward to 2002.

2. The amount included under paragraph 94.1(3)(*a*) in Canco's income for 2002 is nil (A = 25, D = 100). The amount determined under subparagraph 94.1(3)(*b*)(i) for 2002 is 75, which can be carried forward to 2003.

3. The amount included under paragraph 94.1(3)(*a*) in Canco's income for 2003 is 15 (A = 90, D = 75). The amount determined under subparagraph 94.1(3)(*b*)(i) for 2003 is nil.

4. The amount included under paragraph 94.1(3)(*a*) in Canco's income for 2004 is nil (B = 20, D = 0). The amount deductible under paragraph 94.1(3)(*b*) is 15 (= the lesser of 20 and 15). The remaining $5 unused loss allocation can be carried forward to 2005.

5. The amount included under paragraph 94.1(3)(*a*) in Canco's income for 2005 is $45 (A = 50, D = 5).

Example 2

Canco owns shares in the capital stock of FIE-1, which like Canco has a calendar taxation year. Canco's income (loss) allocations for 2001, 2002, 2003, 2004 and 2005 are: (100), (125), (175), 300 and 150.

Results

1. The amount included under subsection 94.1(3) in Canco's income for 2001 is nil (B = 100). The amount determined under subparagraph 94.1(3)(*b*)(i) for 2001 is 100 (= B), which can be carried forward to 2002.

2. The amount included under paragraph 94.1(3)(*a*) in Canco's income for 2002 is nil (B = 125, D = 100). The amount determined under subparagraph 94.1(3)(*b*)(i) for 2002 is 225 (= B+D), which can be carried forward to 2003.

3. The amount included under paragraph 94.1(3)(*a*) in Canco's income for 2003 is nil (B = 175, D = 225). The amount determined under subparagraph 94.1(3)(*b*)(i) for 2003 is 400 (= B+D).

4. The amount included under paragraph 94.1(3)(*a*) in Canco's income for 2004 is nil (A = 300, D = 400). The amount deductible under paragraph 94.1(3)(*b*) is nil (= the lesser of 100 and nil). The remaining $100 unused loss allocation (= D - A) can be carried forward to 2005.

5. The amount included under paragraph 94.1(3)(*a*) in Canco's income for 2005 is $50 (A = 150, D = 100).

Example 3

1. Canco, FIE-1 and ABC Inc. each have taxation years that coincide with calendar years and each issue only one class of shares.

2. Canco is a corporation resident in Canada that holds 20% of the shares of the capital stock of an FIE (FIE-1).

3. FIE-1 owns 75% of the shares of the capital stock of ABC Inc.

4. ABC Inc. is not an FIE, but would be a controlled foreign affiliate of FIE-1 if FIE-1 were resident in Canada. Although ABC Inc. is a foreign affiliate of Canco, it is not a controlled foreign affiliate of Canco.

5. FIE-1 earns $5,000 in interest income in 2001. It also receives a dividend of $1,000 from ABC Inc.

6. The fair market value of FIE-1's shares in ABC Inc. increases by $6,500 in 2001. This increase in value ignores the $1,000 dividend paid from ABC Inc. (i.e., the increase in value would have been about $1,000 higher if no such dividends had been paid).

Results

1. Under subsection 94.1(3), Canco is required to include in computing income its income allocation in respect of its shares in the capital stock of FIE-1. For this purpose, FIE-1's income is generally computed as if FIE-1 were resident in Canada.

2. FIE-1's income includes the $5,000 of interest income (as per paragraph 12(1)(*c*)). However, the $1,000 dividend from ABC Inc. is disregarded because of paragraph 94.1(5)A(*g*). Because of the reference to section 91 in paragraph 94.1(5)A(*a*), it is not necessary to make any foreign accrual property income calculation in respect of ABC Inc.

3. Canco must therefore include $1,000 (i.e., 20% x $5,000) in computing its income by virtue of subsection 94.1(3).

Example 4

Same facts as in example 3, except that ABC Inc. is itself an FIE.

Results

1. The mark-to-market rules in section 94.2 will apply in the calculation of FIE-1's income in respect of its interest in ABC Inc.. See, in this regard, paragraph 94.1(4)(*e*).

2. For the purpose of computing Canco's income allocation in respect of its shares in FIE-1, FIE-1's income would include the $5,000 of interest (as per example 3), but not include any share of foreign accrual property income (as per example 3). However, FIE-1's income would include the $1,000 dividend paid in addition to its gain determined under subsection 94.2(4)

in respect of its participating interest in ABC Inc. This gain so determined is $7,500, which is equal to the $6,500 increase in the value of shares plus the $1,000 dividend paid. However, for the purposes of computing Canco's income allocation, a deduction for the $1,000 dividend is permitted for FIE-1 because subsection 94.3(2) would have permitted the deduction if FIE-1 had been resident in Canada.

3. Consequently, Canco's income allocation in respect of its shares of the capital stock of FIE-1 is equal to $2,500 [i.e., ($5,000 + $7,500 + $1,000 - $1,000) x 20%)]. This amount is required to be included in computing Canco's income under subsection 94.1(3).

ITA
94.1(7)

A taxpayer's "loss allocation" in respect of the taxpayer's participating interest in an entity is relevant for the purposes of determining the amounts deductible and included in computing income under new subsection 94.1(3) of the Act. In general, a taxpayer's loss allocation in respect of an FIE is the proportion of the FIE's net loss for the year that the fair market value of the taxpayer's participating interest in the FIE is of the fair market value of all participating interests in the FIE. More specifically, a taxpayer's loss allocation in respect of a participating interest of a taxpayer in an entity for a taxation year of the entity is determined as follows:

- ADD the entity's total losses for the year from businesses and properties,

- SUBTRACT the amount determined under paragraph 3(*c*) for the entity for the year (i.e., the total amount of its income from business and property and taxable capital gains in excess of allowable capital losses for the year), and

- MULTIPLY any positive remainder by the percentage that the fair market value of the interest represents of the fair market value of all participating interests in the entity (other than rights to acquire participating interests).

The determination of a taxpayer's loss allocation is subject to the same special rules that apply for the purposes of computing a taxpayer's income allocation under subsection 94.1(5) (e.g., the entity is generally deemed to be resident in Canada).

ITA
94.1(8)

Under new subsection 94.1(3) of the Act, a taxpayer is entitled to deduct the taxpayer's specified tax allocation in computing income, provided that sufficient amounts are otherwise included under subsection 94.1(3) in computing the taxpayer's income.

A taxpayer's specified tax allocation for an entity's taxation year in respect of a participating interest in an entity is determined under subsection 94.1(8). It represents the total of the taxpayer's shares of "grossed-up" taxes paid by the entity in the entity's year in respect of the entity's liability for income or profits taxes for the entity's year and preceding taxation years of the entity. The taxpayer's share is based on the taxpayer's percentage fair market value interest in the entity at the end of each of the entity's taxation years to which the tax liability relates. The gross-up available to a taxpayer is equal to 163% for corporations and 100% for individuals, as a result of the taxpayer's share of income profits being multiplied by the relevant tax factor (2.63 for corporations and 2 for individuals).

Income or profits tax is normally expected to be tax that is paid by an entity to a foreign government. However, it could also include income tax paid to the government of Canada or a province with respect to income earned by the entity from Canadian sources. In each case, only income or profits tax payable for taxation years of entities that end in a taxation year of a taxpayer that begins after 2000 is taken into account.

The example below illustrates the operation of subsections 94.1(3) and (8).

Example

In 1998, Mireille (a resident of Canada) purchased a 30% participating interest in an entity (FIE-1) that is an FIE. The rate of foreign tax applicable to FIE-1's income is 20%. FIE-1's taxation years coincide with calendar years. For the purposes of computing Mireille's income allocation and loss allocation in respect of the interest, the income (loss) and the foreign tax of FIE-1 for taxation years 2001 to 2004 are as follows:

Year	2001	2002	2003	2004	Total
Income (loss)	$ 100,000	(120,000)**	$95,000	$130,000	$205,000
Foreign tax paid*	$20,000	Nil	Nil	$21,000	$41,000

* Assume foreign tax paid in the same taxation year as liability arose.

** Assume that an equivalent amount is carried forward under the laws of the relevant foreign jurisdiction to reduce FIE-1's tax liabilities after 2002.

Results

Mireille's income allocations, loss allocations and specified tax allocations are shown in the table below, as are the resulting income inclusions and deductions under subsection 94.1(3). The specified tax allocations in the table below are obtained by multiplying the related figures in the above table by 30% (Mireille's percentage interest) and 2 (specified tax factor for Mireille). For example, for 2001 Mireille's specified tax allocation is $12,000 ($20,000 x 30% x 2).

Year	2001	2002	2003	2004
A. Income allocation	$30,000	nil	$28,500	$39,000
B. Specified tax allocation	$12,000	nil	nil	$12,600
C. Loss allocation (used)	nil	$18,000	nil	nil
D. Carry-forward offset used	nil	nil	$18,000	nil
E. Loss allocation/ tax allocation to carryforward	nil	$18,000	nil	nil
Amount included in income under subsection 94.1(3) (A - B - C - D)	$18,000	nil	$10,500	$26,400
Amount deducted in computing income under subsection 94.1(3) (D + C + B - A)	nil	$18,000	nil	nil

ITA
94.1(9)

New subsection 94.1(9) of the Act provides for adjustments to the adjusted cost base (ACB) of a participating interest in an entity held by a taxpayer.

Paragraph 94.1(9)(*a*) provides for an addition to the ACB of a participating interest held by a taxpayer at the end of a taxation year of the entity, in respect of an amount included in computing the taxpayer's income under subsection 94.1(3) in respect of the interest and the year. Conversely, paragraph 94.1(9)(*b*) provides for a reduction to the ACB of a participating interest held by a taxpayer at the end of a taxation year of the entity, in respect of amounts deducted in computing the taxpayer's income under subsection 94.1(3) in respect of the interest and the year.

ITA
94.1(10) and (11)

New subsections 94.1(10) and (11) of the Act are relevant in determining whether a non-resident entity is an FIE. A non-resident entity is generally an FIE at any time if the carrying value of all of the entity's "investment property" is more than 50% of the "carrying value" of all its property at the end of the entity's taxation year that includes that time.

Where at any time an entity has a "significant interest" (as described below) in a corporation, partnership or non-discretionary trust, in determining the carrying value at that time of the entity's property, the carrying values of the entity's "participating interests" (as described in the commentary above) in the corporation, trust or partnership are deemed to be nil. Debt that is investment property (and that is owing to the entity by the corporation, partnership or trust) is also deemed to have a carrying value to the entity of nil. Instead, the entity is deemed to own the property of the corporation, trust or partnership. Each such property is deemed to have a carrying value to the entity based on the product of the property's carrying value to the corporation, trust or partnership and a percentage based on:

- the entity's percentage relative ownership (determined with reference to fair market value) of shares or interests in the corporation, partnership or trust, as the case may be, and

- the entity's percentage relative ownership (determined with reference to fair market value) in debt issued by the corporation, partnership or trust (other than debts that are not investment property), as the case may be.

Subsection 94.1(10) is intended to operate on an iterative basis. Thus, if there are tiers of entities each of which has a significant interest in the other, the intended effect of subsection 94.1(10) is to deem higher tier entities to own properties of lower tier entities on an iterative basis. For example, assume a non-resident entity (Foreignco-1) owns 100% of the shares in Foreignco-2 which in turn only owns 100% of shares in Foreignco-3 and that Foreignco-1, Foreignco-2 and Foreignco-3 have identical taxation year ends. The carrying values from properties in Foreignco-3 would, under subsection 94.1(10), become the carrying values of properties in Foreignco-2. Because subsection 94.1(10) operates on an iterative basis, the carrying value of those properties would be considered to be the carrying values of properties held by Foreignco-1.

New subsection 94.1(11) sets out the circumstances in which an entity is considered to have a "significant interest" in a corporation, partnership or non-discretionary trust for the purposes of subsection 94.1(10). An entity is considered to have a significant interest in a corporation, partnership, or non-discretionary trust where it holds shares or interests in the corporation, partnership or trust that have a fair market value equal to 25% or more of the fair market value of all the shares or interests in the corporation, partnership or trust and, in the case of a corporation the entity has shares entitling the entity to cast at least 25% of votes at an annual shareholders' meeting of the corporation.

The example below illustrates the operation of subsection 94.1(10).

Example

1. Jean, who resides in Canada, holds a participating interest in Foreignco, a non-resident corporation that is not a controlled foreign affiliate of Jean. Foreignco's principal activity is the carrying on of investment activities on behalf of its shareholders. Foreignco prepares its financial statements in accordance with accounting principles substantially similar to generally accepted accounting principles used in Canada.

2. The carrying values of Foreignco's assets at the end of its taxation year ending in the taxpayer's year are as follows:

guaranteed investment certificate	$10,000
shares of XYZ Inc. in which Foreignco has a significant interest	$20,000
shares of ABC Inc. in which Foreignco does not have a significant interest	$ 5,000
cash	$ 4,000
Total assets	$39,000

3. XYZ Inc. owns assets at that time that are used in the course of carrying on an active business, with a carrying value of $80,000. It also has investment property with a carrying value of $15,000.

4. The fair market value of the shares of XYZ Inc. held by Foreignco is $40,000 while the fair market value of all the issued and outstanding shares of XYZ Inc. is $100,000 at that time.

Results

1. The guaranteed investment certificate, cash, and the shares of XYZ Inc. and ABC Inc. are all investment property by virtue of the definition "investment property" in subsection 94.1(1).

2. However, since Foreignco owns a significant interest in XYZ Inc., the special look-through rule in new subsection 94.1(10) applies. Under this look-through rule the carrying value of Foreignco's shares in XYZ Inc. is deemed to be nil. Instead, Foreignco is deemed to own the property that XYZ Inc. owns.

3. The carrying value of the XYZ property deemed to be owned by Foreignco is 40% of its carrying value to XYZ, since Foreignco's percentage ownership of shares is 40%.

4. Consequently, the carrying values of the investment property of Foreignco are:

guaranteed investment certificate	$10,000
shares of XYZ Inc.	nil
shares of ABC Inc.	$ 5,000
cash	$ 4,000
investment property of XYZ Inc. (40% of $15,000)	$ 6,000
Total	$25,000

5. The total carrying value of the assets of Foreignco is:

Investment property (see above)	$ 25,000
assets of XYZ Inc. (other than investment property) (40% of $80,000)	$ 32,000
Total	$ 57,000

6. As a result, Foreignco is not an FIE because less than 50% of the carrying value of its property is investment property.

ITA
94.1(12)

New subsection 94.1(12) of the Act permits a taxpayer to make an irrevocable election to treat its foreign affiliate (including an affiliate the shares which are held by the taxpayer's controlled foreign affiliate) as a controlled foreign affiliate for a particular taxation year and subsequent taxation years. This one-time election is available only if:

- a taxation year of the affiliate ends at or before the end of the particular year,
- the taxpayer has a "qualifying interest" (as defined in paragraph 95(2)(*m*)) in the affiliate, and

- the principal business of the affiliate is an excluded investment business or a business that is not an investment business (as defined in subsection 94.1(1)).

The election must be made in prescribed form in the taxpayer's tax return for the year. However, under subsection 94.1(17), the election may be rendered invalid in the event that the taxpayer cannot provide sufficient information to the Minister of National Revenue for the Minister to be able to determine amounts required to be included in the taxpayer's income under section 91. In addition, the election no longer has any effect if the corporation ceases to be a foreign affiliate of the taxpayer or once the entity's principal business is an investment business (other than an excluded investment business).

In the period during which such an election is effective, a foreign affiliate of a taxpayer is deemed to be a controlled foreign affiliate of the taxpayer. As a result, a share issued by the affiliate to the taxpayer would be an "exempt interest" under the definition in subsection 94.1(1). Sections 94.1 and 94.2 generally would not apply to the taxpayer's participating interest in the affiliate. However, the foreign accrual property income (FAPI) rules would apply and the taxpayer would be required to include in income under section 91 a percentage of any FAPI derived by the affiliate in the year. Notwithstanding an election under subsection 94.1(12), section 94.2 may still apply in the event that a taxpayer's interest in a controlled foreign affiliate is a tracked interest to which subsection 94.2(9) applies.

ITA
94.1(13) to (15)

New subsection 94.1(13) of the Act provides a special rule under which investment property is deemed to have a carrying value of nil.

Subsection 94.1(13) applies where there is a "qualifying disposition" (as defined in subsection 94.1(14)) or a "qualifying issue" (as defined in subsection 94.1(15)).

A "qualifying disposition" of an entity occurs where the entity disposes of all or substantially all of its assets used or held in a business (other than an investment business, as defined in the commentary above) in an arm's length transaction, either in a single transaction or as part of a series of transactions or events.

A "qualifying issue" of an entity is essentially an issue to a person or partnership of a debt or participating interest, but with the qualification that a qualifying issue does not arise if the issue is part of a series of transactions or events that also includes the disposition of a debt or participating interest in the entity (or another non-arm's length entity) by the same person or partnership (or certain other non-arm's length parties). This qualification is meant to prevent the circular flow of funds from and to an entity giving rise to a "qualifying issue".

Where an entity has a "qualifying disposition" or "qualifying issue", the consideration received by the entity (cash, shares, and debt) will in most cases be "investment property", as defined in subsection 94.1(1). As a result, the entity (or another entity that has a significant interest in the entity) might otherwise become an FIE. To allow a potential grace period before an entity is classified as an FIE, investment property received as consideration received on the sale of the business or on a qualifying issue (and each investment property substituted for the investment property so received) is deemed, at the end of the taxation year in which the qualifying disposition or qualifying issue took place, to have a carrying value of nil.

ITA
94.1(16) and (17)

New subsections 94.1(16) and (17) of the Act provide for the application of the mark-to-market rules in section 94.2 to a participating interest in an FIE, if insufficient information is available to determine amounts required to be added or deducted in a taxpayer's income in respect of the interest under subsection 94.1(3). The information required for this purpose would include a calculation of taxable capital gains from dispositions, calculated in Canadian dollars and with reference to the assumptions for the calculation of income set out in subsection 94.1(5).

If this information is not made available to the Minister on a timely basis on demand in respect of a participating interest in an entity, subsection 94.1(17) effectively provides that the rules in section 94.2, rather than the rules in section 94.1, apply in respect of the entity.

Similar rules apply in the event that insufficient information is provided to enable the appropriate calculation of a taxpayer's income arising from an election under subsection 94.1(12). The latter election would otherwise permit an affiliate to be treated as a controlled foreign affiliate. If insufficient information is provided in this context, the mark-to-market rules in section 94.2 will generally apply to the taxpayer if the affiliate is an FIE.

ITA
94.2

New section 94.2 of the Act sets out new rules for the taxation of interests in FIEs.

Except as otherwise indicated, section 94.2 applies to taxation years of investors that begin after 2000.

ITA
94.2(1)

New subsection 94.2(1) of the Act provides that the definitions in subsection 94.1(1) apply for the purposes of section 94.2.

Subsection 94.2(1) also sets out the definitions "deferral amount" and "gross-up factor".

The deferral amount of a taxpayer generally represents the gain or loss (or, in the event that the interest was capital property held by the taxpayer on **ANNOUNCEMENT DATE**, two-thirds of the gain or loss) in respect of the interest accrued to the time when the interest first became subject to the operation of the rules in section 94.2. The expression "deferral amount " in respect of a participating interest in an entity applies principally for the purpose of determining the value of D in the formula set out in subsection 94.2(4). Subsection 94.2(4) generally provides for the recognition of a deferral amount in respect of a participating interest on the disposition of the interest. Because of subsection 94.2(2), identical participating interests are considered to be disposed of in the order in which they were acquired.

For participating interests in FIEs acquired after 2000, each deferral amount will be nil in the typical cases where the rules in section 94.2 apply to a taxpayer's interest in an FIE for the year in which the interests were acquired.

The deferral amount is calculated, in conjunction with subsections 94.2(5) and subsection 128.1(4), so that gains and losses accruing while a taxpayer is not resident in Canada are ignored for the purposes of section 94.2, except in the unusual case where an interest in an FIE is taxable Canadian property.

Additional rules affecting the calculation of the deferral amount are contained in subsections 94.2(6) and (13) to (17), as described in the commentary below.

The "gross-up factor" for a deferral amount is 1, except where the 2/3 factor is relevant in computing the deferral amount. In the latter case, the "gross-up factor" is the reciprocal of the 2/3 factor (i.e., 3/2). For detail on the relevance of this definition, see the commentary on subsection 94.2(11).

ITA
94.2(2)

New subsection 94.2(2) of the Act provides rules of application for the purpose of section 94.2.

Paragraph 94.2(2)(*a*) provides that identical properties held by a taxpayer are deemed to be disposed of in the order in which they were acquired by the taxpayer. For this purpose, paragraph 94.2(2)(*a*) makes it clear that the various acquisitions that are deemed to occur under the Act (e.g., section 47) are not to be taken into account. This measure is relevant primarily for the purpose of determining the amount added or deducted from a taxpayer's income under subsection 94.2(4), especially with reference to the "deferral amount" referred to in the description of D in paragraph 94.2(4)(*a*).

Paragraph 94.2(2)(*b*) provides that the rules in subsections 94.1(10) and (11) (look-through rule for significant interests) also apply for the purposes of section 94.2. This measure is significant for the purposes of applying subsection 94.2(9) (tracked interests).

ITA
94.2(3) and (4)

Subsection 94.2(3) of the Act sets out those circumstances where, subject to paragraph 94.2(5)(*b*), subsection 94.2(3) applies to a taxpayer in respect of a participating interest in a non-resident entity. For the mark-to-market regime in subsection 94.2(4) to apply for a taxation year, subsection 94.2(3) must apply for the year.

For subsection 94.2(3) to apply to a taxpayer throughout a taxation year in respect of a participating interest in a non-resident entity, either:

- Subsection 94.1(2) applies to the taxpayer for the year in respect of the interest, but not result in the application of the accrual regime under subsection 94.1(3) because of the application of subsection 94.1(4). (For details, see the commentary on subsections 94.1(2) and (4).); or
- Subsections 94.2(9) (tracked interests) or 94.2(10) (foreign insurance policies) apply to the taxpayer for the year in respect of the interest.

Where subsection 94.2(3) applies to a participating interest in an FIE, paragraph 94.2(4)(*a*) requires a taxpayer to include in computing income, in respect of the interest, any positive amount resulting from the operation of the formula set out in paragraph 94.2(4)(*a*). Under paragraph 94.2(4)(*b*), the absolute value of any negative amount resulting from the operation of the same formula may be deducted in computing the taxpayer's income. (Note, however, that losses in respect of foreign insurance polices are denied because of subparagraph 94.2(4)(*b*)(i). Instead, as described below, the denied losses are carried forward to offset later income inclusions.)

The amount determined under the formula for a taxpayer's taxation year in respect of a participating interest in an FIE is computed as follows:

- [A] ADD the proceeds of disposition in the year from any disposition by the taxpayer in the year of the interest (other than a disposition arising from the application of subsection 128.1(4) or 149(10), given that the value of B would take into account the fair market value of the interest at the time of such deemed dispositions);

- [B] where the taxpayer held the interest at the end of the year, ADD the fair market value of the interest at that time (determined before taking into account the FIE's liability in respect of any amount payable from the FIE in respect of the interest);

- [C] ADD the total payments received by the taxpayer in the year from the FIE, other than payments included in the value of A;

- [D] where the taxpayer so elects for a year during which the taxpayer did not dispose of the interest, ADD any positive deferral amount in respect of the interest;

- [D] where the taxpayer disposed of the interest in the year and the election referred to above has not been previously made, ADD the deferral amount in respect of the interest;[28]

- [E] SUBTRACT the cost of the interest on any acquisition in the year of the interest (disregarding acquisitions arising because of the application of subsection 128.1(4) or 149(10), given that these acquisitions are taken into account in the value of F);

- [F] where the taxpayer held the interest at the beginning of the year, SUBTRACT the fair market value of the interest; and

- [G] in the case of a foreign insurance policy to which subsection 94.2(3) applies because of the operation of new subsection 94.2(10), SUBTRACT any loss denied for the preceding year because of the operation of subparagraph 94.2(4)(*b*)(*i*).

Ignoring the descriptions of D and G, the formula in paragraph 94.2(4)(*a*) in effect determines the net increase or decrease in the fair market value of a taxpayer's participating interest in an FIE for a taxation year.

The value of D represents a taxpayer's accrued gain or loss when a participating interest first becomes subject to section 94.2. The amount of this accrued gain or loss (or two-thirds of it, in the event so provided in the definition "deferral amount" in paragraph 94.2(1)(*b*)) is included in computing income under the description of D, but only for the taxation year in which the interest is disposed of unless the taxpayer elects for earlier recognition of a positive deferral amount. (An earlier recognition of a positive deferral amount may be beneficial for a taxpayer, particularly where section 94.3 applies.) Where the taxpayer is a trust, a disposition may occur as a consequence of the application of the 21-year deemed disposition rule. See, in this regard, new subsection 104(4.1).

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[28] The value of D will reduce the amount determined under the formula in the event that the deferral amount is a negative amount.

The example below illustrates the operation of subsection 94.2(4).

Example

1. Leonard acquires a 1% interest in ABC Inc. in 1999 for $500. On **ANNOUNCEMENT DATE**, it is capital property to Leonard. ABC Inc. is not an FIE in respect of the taxpayer at any time before 2003.

2. ABC Inc. becomes an FIE during 2003 and Leonard does not elect under subsection 94.1(4) to have the rules in section 94.1 apply. Leonard's interest in ABC Inc. does not qualify as an "exempt interest".

3. The fair market values of Leonard's participating interest at the beginning and at the end of year 2003 are $800 and $1,000 respectively.

4. Leonard disposes of his shares just before the end of 2004 for $1,200. ABC Inc. does not make any distributions to Leonard during his period of ownership.

Results

1. No amount is included in Leonard's income for 2001 and 2002 under either section 94.1 or 94.2. For 2003, Leonard is required to include $200 in income under the formula in paragraph 94.2(4)(*a*).

2. The $200 inclusion is determined as follows:

    - "A" is nil, since no participating interest in ABC Inc. is disposed of in 2003,
    - "B" is $1,000, the fair market value of the participating interest at the end of 2003,
    - "C" is nil since no payments are received in 2003,
    - "D" is nil since no participating interest is disposed of in 2003 and no election was otherwise made,
    - "E" is nil since no participating interest in ABC Inc. is acquired in 2003, and
    - "F" is $800, the fair market value of the participating interest at the beginning of 2003.

3. Although Leonard's participating interest has appreciated by $500 since the time of its acquisition, only $200 is required to be included in income under section 94.2 for 2003.

4. For 2004, the amount included in income under subsection 94.2(4) is $400, computed as follows:

    - "A" is $1,200, the proceeds of disposition of the participating interest,
    - "B" is nil since Leonard does not own any participating interest in ABC Inc. at the end of 2004,
    - "C" is nil since no payments or distributions were received in 2004,
    - "D" is $200, the deferral amount in respect of the interest – the "deferral amount" is two-thirds[29] of the amount by which $800 (the fair market value of the interest at the beginning of 2003 which is the first year in respect of which section 94.2

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[29] The two-third factor applies because Leonard's interest in ABC Inc. is capital property held by Leonard on **ANNOUNCEMENT DATE**.

applies to the interest) exceeds $500 (the cost amount of the interest),

- "E" is nil since no participating interest in ABC Inc. is acquired in 2004, and
- "F" is $1,000, the fair market value of the participating interest at the beginning of 2004.

ITA
94.2(5)

New subsection 94.2(5) of the Act provides special rules dealing with the application of section 94.2 for a taxation year to persons who are not resident in Canada throughout the year.

Under paragraph 94.2(5)(*a*), the amounts determined under section 94.2 are generally determined as if the taxation year of such a taxpayer excludes the period in the year during which the taxpayer is not resident in Canada. This rule, in conjunction with section 128.1, generally ensures that the increases and decreases in fair market values that are relevant in determining income inclusions and deductions under section 94.2 are the increases and decreases occurring while the taxpayer is resident in Canada. However, this rule does not affect the calculation of the taxpayer's deferral amount: paragraph 94.2(1)(*b*) (in conjunction with subsection 128.1(1)) already ensures that gains or losses accruing prior to becoming resident in Canada are not taken into account for the purposes of computing a taxpayer's deferral amount in respect of a participating interest in an FIE, except in the unusual case where the FIE interest is taxable Canadian property.

Paragraph 94.2(5)(*a*) also ensures that subsection 94.2(4) does not apply to a taxpayer for a taxation year throughout which the taxpayer is not resident in Canada.

Under paragraph 94.2(5)(*b*), subsection 94.2(3) generally does not apply to a taxpayer at a particular time if the taxpayer is not resident in Canada at the particular time. This has relevance for the purposes of a number of new provisions, including subparagraph 39(1)(*a*)(ii.3). This subparagraph has the effect of excluding, from a taxpayer's capital property, a property in respect of which subsection 94.2(3) applies and is intended to ensure that there is no double taxation with respect to the same economic gain. Paragraph 94.2(5)(*b*) thus ensures that a non-resident taxpayer cannot claim that a taxable Canadian property consisting of an FIE interest is not capital property on the basis of subparagraph 39(1)(*a*)(ii.3). (Note: non-resident taxpayers are generally subject to tax on taxable capital gains from their dispositions of taxable Canadian properties.)

Paragraph 94.2(5)(*c*) applies in the unusual case where an individual changes his or her Canadian residence status more than once in the same calendar year. For example, an individual might leave Canada near the beginning of a calendar year but return later in the same year. In the event that such an individual is considered not to reside in Canada during a period in the calendar year, the individual's period of non-residence would be included within the individual's taxation year and the rule in paragraph 94.2(5)(*a*) would have no effect. In order to not tax gains accrued while an individual was non-resident and to not provide relief for losses accrued during the same period, paragraph 94.2(5)(*c*) provides:

- for the purposes of section 114, the individual's income or loss from the individual's period of non-residence is determined without reference to section 94.2, and

- in computing the individual's taxable income under section 114,

    - there is deducted the fair market value appreciation of an interest in an FIE to which subsection 94.2(4) applies during the non-resident period (this fair market value appreciation would be reflected in the amount determined under subsection 94.2(4) in computing the taxpayer's income), and

    - there is added the fair market value decline of an interest in an FIE to which subsection 94.2(4) applies during the non-resident period (this fair market value decline would be reflected in the amount determined under subsection 94.2(4) in computing the taxpayer's income).

The example below illustrates the operation of paragraph 94.2(5)(*c*).

Example

Bernard emigrates from Canada on February 1, 2001 in order to start permanent employment elsewhere. After the position does not work out, he returns to Canada on December 1, 2001. Bernard owns an interest in an FIE to which section 94.2 applies. The fair market value of the interest in 2001 is $100 (January 1, 2001), $105 (February 1, 2001), $108 (December 1, 2001) and $107 (December 31, 2001). It is assumed that Bernard establishes that he did not reside in Canada from February 1, 2001 to December 1, 2001.

Results

1. Under section 94.2(4), the amount included in computing Bernard's income for 2001 is equal to $7 (B = 107, F = 100).

2. Paragraph 94.2(5)(*c*) permits a deduction for the purposes of paragraph 114(*a*) equal to $3 (i.e., $108 - $105) equal to the appreciation in the fair market value of the interest while Bernard was not resident in Canada. As a consequence, Bernard's taxable income in respect of the FIE interest for 2001 is equal to $4 (i.e., $7 minus $3).

ITA
94.2(6) to (8)

New subsections 94.2(6) to (8) of the Act provide special rules for partnerships having non-resident members. These subsections are analogous to rules in existing subsections 96(8) and (9) and are designed, in general terms, to prevent partnership losses that accrue while no partnership member is resident in Canada from being used in Canada. A further rule for partnership members is set out in new subsection 96(1.9).

More specifically, subsection 94.2(6) applies where a partnership begins to have members who reside in Canada. Under subsection 94.2(7), a corresponding rule applies in a similar fashion where a partnership ceases to have members who reside in Canada. In either case, for the purposes of determining amounts under section 94.2 portions of the fiscal period of the partnership in which no member is resident in Canada will generally be disregarded.

Where subsection 94.2(6) applies to a partnership at any time, the deferral amount for an FIE interest held by the partnership immediately before that time is computed with reference to the fair market value and the cost amount of the interest. However, if a negative deferral amount is otherwise determined with respect to the interest, the deferral amount is deemed to be nil.

As a consequence of subsections 94.2(6) and (7), amounts added or deductible under subsection 94.2(4) for a partnership in respect of an FIE interest will generally reflect increases or decreases in fair market value while the partnership has members resident in Canada. However, once the interest is disposed of, an amount reflecting gains accruing before any member became resident in Canada will be recognized because of the application of subsection 94.2(4).

Subsection 94.2(8) contains an anti-avoidance rule, which is aimed at preventing the insertion of nominal Canadian resident partners for tax planning purposes. This rule is parallel to the rule in existing subsection 96(9).

Subsection 94.2(8) also contains a look-through rule. It allows for the look-through of one or more tiers of partnerships for the purposes of determining whether a person is a member of a partnership.

ITA
94.2(9)

New subsection 94.2(9) of the Act is an anti-avoidance rule intended to prevent the circumvention of sections 94.1 and 94.2 through the creation of "tracked interests" in entities that are not FIEs or through the creation of an interest in an FIE that would otherwise be an "exempt interest". Where subsection 94.2(9) applies with regard to a "tracked interest" for a taxation year, the mark-to-market regime in section 94.2(4) applies to a taxpayer for that year.

A participating interest held by a taxpayer in a particular non-resident entity in a taxation year is a "tracked interest" in the particular entity for a particular taxation year of the taxpayer where:

- a taxation year of the particular entity ended at or before the end of the particular year (the latest of which taxation years is referred to below as the "specified year");[30]
- the taxpayer is not an exempt taxpayer for the particular year (see commentary on definition "exempt taxpayer" in subsection 94.1(1));[31]
- the entitlement to receive payments from the particular entity in respect of the participating interest (or its fair market value) is determined primarily by reference to production, revenue, profit or cash flow from, the fair market value or the use of, or any other similar criterion in respect of, a property or group of properties (referred to below as the "tracked properties");[32]
- in the event that all of the tracked properties are properties owned by the particular entity, they do not comprise the totality of the entity's properties.[33] (Note: the deemed ownership rule in subsection 94.1(10) is ignored for the purpose of determining whether this condition is satisfied.);
- either
  - the entity (or any other non-resident entity) owns an investment property (other than a tracked property owned by the entity) and it is reasonable to conclude that the production, revenue, profit or cash flow from that investment property, the increase in the fair market value of that investment property or any other return based on a similar criterion is intended to enable the entity to satisfy all or part of an entitlement in respect of a tracked interest,[34] or
  - in general terms, the total carrying value of investment property owned by the entity that is included in the tracked properties is more than one-half of the total carrying value of all property

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[30] Paragraph 94.2(9)(*b*).

[31] Paragraph 94.2(9)(*c*).

[32] Paragraph 94.2(9)(*d*).

[33] Paragraph 94.2(9)(*e*).

[34] Paragraph 94.2(9)(*f*)(ii).

owned by the entity that is included in the tracked properties.[35]

More specifically, for the purpose of determining the above totals, the carrying value of investment property owned by an entity included in the tracked properties as of the end of the specified year is determined as follows:

- ADD the carrying value of investment property included in the tracked properties and owned by the particular entity (determined with reference to the definition "investment property" and the deemed ownership rule in subsection 94.1(10)); and

- ADD the carrying value (determined without reference to subsection 94.1(10)) of specified investment property owned by the particular entity and included in the tracked properties. The investment property so specified is the property that would otherwise have a deemed cost of nil under paragraph 94.1(10)(*a*) and that is either a participating interest in an FIE or indebtedness owing by an FIE. (The specified investment property represents debt or equity interests in entities in which the particular entity has a "significant interest", as defined by subsection 94.1(11).)

For the same purpose, the total carrying value of the total property included in the tracked properties is determined as of the end of the specified taxation year of the particular entity in the following manner:

- ADD the carrying value of each property owned by the particular entity that is included in the tracked properties. (This determination is made with reference to the look-through rule in subsection 94.1(10).); and

- ADD the carrying value (determined without reference to subsection 94.1(10)) of specified investment property referred to above.

It should be noted that tracked properties can include any property, whether or not owned by a taxpayer or a related group of which the taxpayer is a part. For example, if the fair market value of shares issued by a non-resident entity is tracked to the world-wide price of gold bullion, the tracked properties in question would be the world-wide supply of gold bullion. Whether subsection 94.2(9) applies or not in this case would typically depend on whether subparagraph 94.2(9)(*f*)(ii) applies to the non-resident entity.

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[35] Paragraph 94.2(9)(*f*)(i).

It should also be noted that there is no exemption under subsection 94.2(9) with regard to an "exempt interest" (as defined in subsection 94.1(1)) in a non-resident entity. Thus, the mark-to-market rules can apply to a taxpayer in respect of shares of the capital stock of a controlled foreign affiliate of the taxpayer.

ITA
94.2(10)

New subsection 94.2(10) of the Act sets out the treatment under section 94.2 of an interest in a foreign insurance policy. For this purpose, a foreign insurance policy is one that is neither

- issued by an insurer in the course of carrying on business in Canada the income from which is subject to tax under Part I, nor

- entered into solely in respect of risks that relate to activities occurring outside Canada or losses in respect of tangible property ordinarily situated outside Canada.

Paragraph 94.2(10)(*a*) generally provides that, where a taxpayer (other than an exempt taxpayer) holds an interest in such an insurance policy, for the purposes of subsections 94.2(3) and (4) (and a corresponding foreign property reporting rule in subsection 233.3(1)) the particular interest is deemed to be a participating interest in a non-resident entity to which the mark-to-market rules in subsection 94.2(4) apply. However, the mark-to-market regime under subsection 94.2(4) applies differently to insurance policies in two respects. First, no deferral amount is calculated with regard to insurance policies. Second, losses are not deductible, but instead can be used to offset future income amounts otherwise arising under subsection 94.2(4). (As to the treatment of losses, see the commentary on subsection 94.2(4).) Paragraph 94.2(10)(*a*) also provides that, where the mark-to-market rules apply to an insurance policy, the other rules in the Act with regard to the taxation of insurance products do not apply.

Under paragraph 94.2(10)(*b*), paragraph 94.2(10)(*a*) does not apply in connection with a policy an interest in which was acquired more than five years before a taxpayer became resident in Canada. However, this exception does not apply if premiums in excess of the level originally contemplated under the policy have been paid within 5 years of the policyholder becoming resident in Canada or while the policyholder was resident in Canada.

In the event that an insurance policy is subject to paragraph 94.2(10)(*a*) for one taxation year but not subject to that paragraph for the preceding year, paragraph 94.2(10)(*c*) provides that the taxpayer is deemed, at the end of the preceding year, to have disposed of the taxpayer's interest in the insurance policy at its fair market value (determined with reference to paragraph 94.2(10)(*e*)).

In the event that an insurance policy is subject to paragraph 94.2(10)(*a*) for one taxation year but not subject to that paragraph for the following year, paragraph 94.2(10)(*d*) provides that the taxpayer is deemed, at the beginning of the following year, to have acquired the taxpayer's interest in the insurance policy at its fair market value (determined with reference to paragraph 94.2(10)(*e*)).

Paragraph 94.2(10)(*e*) provides that the fair market value of an interest in an insurance policy and other relevant amounts are determined without reference to benefits paid, payable and anticipated to be payable under the policy only as a consequence of a death, sickness, disability or other prescribed event. (Note: Presently, it is not anticipated that events will be prescribed for this purpose.)

Example

Assume that David, a long-term resident of Canada, pays premiums of $10,000 to an offshore insurer for a life insurance policy. The policy's cash surrender value is $9,000 and $10,700 at the end of 2002 and 2003 (respectively).

Results

1. For 2002, no amount is determined under paragraph 94.2(4)(*a*) because the cost of the policy exceeds the fair market value at the end of 2002.

2. No loss is permitted to be claimed under paragraph 94.2(4)(*b*). The amount of the denied loss is equal to $1,000.

3. For 2003, the amount included in income under paragraph 94.2(4)(*a*) is $700 (= $10,700 ("B"), minus $9,000 ("F"), minus $1,000 ("G")).

4. It should be noted, however, that it is possible that the fair market value could be higher that a policy's cash surrender value. This might be the case, for example, if cash surrender values under a policy were not provided on a consistent basis over time. If this were the case, the fair market value of a policy would be a question of fact.

Subsection 94.2(10), unlike the rest of section 94.2, is to apply to taxation years that begin after 2001.

ITA
94.2(11)

New subsection 94.2(11) of the Act sets out rules that apply where a taxpayer holding a participating interest in an entity was subject to subsection 94.2(4) for a taxation year but is not subject, in respect of the interest, to subsection 94.2(4) for the following taxation year (otherwise than because the taxpayer ceased to reside in Canada or became an "exempt taxpayer", as defined in subsection 94.1(1)).

Where subsection 94.2(11) applies, the taxpayer is deemed to have acquired the particular interest at the beginning of the following taxation year at a cost equal to the fair market value of the particular interest at that time.

The subsection could apply, for example, where a taxpayer holds a share of the capital stock of a non-resident corporation and the share is not an "exempt interest", as defined in subsection 94.1(1). Assume that the taxpayer made no election under subsection 94.1(4) for section 94.1 to apply. If the entity subsequently becomes a controlled foreign affiliate of the taxpayer, subsection 94.2(4) would cease to apply.

Since the taxpayer is deemed to have acquired the property at its fair market value at the beginning of the following year, all increases and decreases in the value of the interest from the time of its acquisition are reflected in the taxpayer's cost of the interest for tax purposes. However, only the gain or loss accruing while it was subject to subsection 94.2(4) has been brought into income. The gain or loss in value for the period from the time of acquisition to the time it became subject to subsection 94.2(4) has not been taken into consideration for tax purposes.

Accordingly, paragraph 94.2(10)(*b*) provides for a negative or positive adjustment to the adjusted cost base (ACB) of a participating interest held as capital property. Any positive "deferral amount" (as defined in subsection 94.2(1)) in respect of the interest is deducted in computing the ACB of the interest, but the deduction is grossed-up by one-half in the event that the deferral amount was calculated with reference to two-thirds of the accrued gains. The ACB deduction does not, however, apply in the event that a positive deferral amount has already been taken into account because of an election under the description of D in paragraph 94.2(4)(*a*). The absolute value of any negative deferral amount (or three-halves of it where the 2/3 factor was used in computing the negative deferral amount) is added in computing the ACB of the interest. Where capital property is not involved, a corresponding decrease or increase in cost (rather than adjusted cost basis) is provided under paragraph 94.2(11)(*c*). To the extent that the decrease would otherwise result in a negative cost, the decrease is brought into the taxpayer's income under paragraph 94.2(11)(*c*).

ITA
94.2(12)

New subsection 94.2(12) of the Act provides a rule for determining the cost at a particular time of a participating interest in an entity for a taxation year in the event that the interest is disposed of by the taxpayer in the year.

The cost to the taxpayer immediately before the disposition of the property is deemed to be its fair market value at the beginning of the taxpayer's taxation year. In the event that the property was not held by the taxpayer at that time, its cost immediately before the disposition is its cost determined without reference to subsections 94.2(4) and (12). In identifying property for these purposes, identical properties of a taxpayer are considered to be disposed of on a "first in, first out" basis, as a consequence of the application of subsection 94.2(2).

Under new paragraph (*c*.2) of the definition "cost amount" in subsection 248(1), the cost determined at a particular time for a property under subsection 94.2 (12) is also the "cost amount" of the property at the particular time.

ITA
94.2(13)

New subsection 94.2(13) of the Act generally provides that a "deferral amount" in respect of a property of a taxpayer is deemed to be nil, after the property has been disposed of by the taxpayer at a time when the mark-to-market rules in subsection 94.2(4) applied to the property. This is of relevance to property that is reacquired by a taxpayer. However, subsection 94.2(13) is subject to rules in subsections 94.2(14) to (17).

It should be noted that identical properties of a taxpayer are considered to be disposed of on a "first in, first out" basis as a consequence of the application of subsection 94.2(2).

ITA
94.2(14)

New subsection 94.2(14) of the Act covers the case where a taxpayer's participating interest in an entity was initially subject to the rules in subsection 94.2(4) and ceases to be subject to those rules (otherwise than because of the taxpayer having become an "exempt taxpayer"). For example, subsection 94.2(14) could apply where an entity loses its status as an FIE.

In these circumstances, the deferral amount in respect of the participating interest is determined without reference to the past application of subsections 94.2(4) and (13). This rule is relevant only in the event that the same participating interest of the taxpayer again becomes subject to the rules in subsection 94.2(4).

Parallel "fresh start" rules are contained in subsection 94.2(15) and (16). All of these "fresh start" rules are expected to be only rarely invoked, given that more than one change in status of an investment or a taxpayer is required for the rules to become relevant. For further detail on the "deferral amount" defined in subsection 94.2(1), see the commentary on that definition.

ITA
94.2(15)

New subsection 94.2(15) of the Act affects the calculation of the "deferral amount" in respect of a participating interest in an entity for a taxpayer who has ceased to reside in Canada. It is relevant in the event that, at a subsequent time, the taxpayer becomes resident in Canada again.

In these circumstances, the deferral amounts in respect of the taxpayer's FIE interests are determined without reference to the past application of subsections 94.2(4) and (13).

For further context, see the commentary above on the related fresh start rule in subsection 94.2(14).

ITA
94.2(16)

New subsection 94.2(16) of the Act affects the calculation of the "deferral amount" in respect of an interest in an entity for a taxpayer that initially was not an "exempt taxpayer" under paragraph (*b*) of that definition and then subsequently both obtains and loses that status.

In these circumstances, the deferral amounts in respect of the FIE interests of the taxpayer are determined without reference to the past application of subsections 94.2(4) and (13).

For further context, see the commentary on the related fresh start rule in subsection 94.2(14). In addition, it should be noted that amended subsection 149(10) applies to changes of tax-exempt status for taxpayers that are corporations. Where subsection 149(10) applies, the rules in subsection 94.2(16) do not apply.

ITA
94.2(17)

New subsection 94.2(17) of the Act applies where a taxpayer disposes of a participating interest in an entity in respect of which a negative amount is determined under the description of D in the formula in subsection 94.2(4). This would be the case where there is a negative deferral amount associated with the interest. In these circumstances, the deferral amount is instead generally deemed to be nil if, during the period beginning 30 days before the disposition and ending 30 days after the disposition, identical property is acquired by the taxpayer or certain related persons.

Subsection 94.2(17) operates in a manner similar to the "superficial loss" rules for capital properties and is intended to prevent the premature realization of losses in respect of a property in which a taxpayer effectively retains an economic interest. "Superficial loss" has the same meaning as assigned in section 54, except that the definition for the purposes of subsection 94.2(17) does not contain the exception for transactions covered by subsection 40(3.4).

Property substituted for the particular property is, in these circumstances, considered to have the deferral amount associated with the property disposed of.

ITA
94.3

Where a taxpayer resident in Canada has received a payment (a dividend, for example) in respect of a participating interest in an entity held by the taxpayer (otherwise than as consideration for the disposition of the interest), new section 94.3 of the Act permits a deduction designed to offset any net income inclusion resulting from the payment. The permitted deduction for a taxation year is equal to the lesser of:

- the amount included (otherwise than because of subsection 94.2(4)) in computing the taxpayer's income for the year in respect of the payment, less any increase in amounts deductible under subsection 91(5) or section 113 caused by the making of the payment, and

- the net amount included in computing the taxpayer's income under sections 94.1 and 94.2 in respect of the participating interest, less deductions for the taxpayer under subsection 94.3(2) in respect of previous payments in respect of the interest.

In the event that the participating interest is capital property, the amount deducted from income under subsection 94.3(2) in respect of the interest is also required to be deducted in computing the adjusted cost base of the interest. Note that this deduction is not of relevance to property to which the mark-to-market rules in section 94.2 apply, given that such property will not be capital property as a consequence of the application of subparagraph 39(1)(*a*)(ii.3) and section 94.2.

Section 94.3 also allows income inclusions in respect of amounts payable (for example, amounts payable by an FIE that is a trust) to be similarly treated.

The example below illustrates the operation of section 94.3.

Example

1. A taxpayer resident in Canada, Canco, purchases a 20% interest in Foreignco, a non-resident corporation. Foreignco is an FIE. Participating interests in Foreignco do not qualify as "exempt interests". Both Canco and Foreignco have taxation years that coincide with calendar years. Canco makes an election under subsection 94.1(4) to have section 94.1 apply.

2. Canco's income allocation in respect of its participating interest in Foreignco for 2001 is $100,000, which is added in computing Canco's income under subsection 94.1(3). This is partially offset by a specified tax allocation of $30,000. Foreignco pays a dividend of $50,000 to Canco in 2001. Canco includes the dividend in income pursuant to section 90 and claims a deduction of $20,000 in computing its taxable income pursuant to subsection 113(1).

Results

1. Canco's deduction from income under section 94.3 is equal to $35,000, being the lesser of the net income inclusion as a result of the payment (= $50,000 minus $20,000) and the amount of

the net income inclusions under subsection 94.1(3) ($100,000 minus $30,000).

2. The result would generally be the same if the $50,000 dividend were instead paid in a subsequent year.

Clause 12

ITA
95(1)

Subsection 95(1) of the Act sets out definitions that are relevant for the purposes of sections 90 to 95.

Subsection 95(1) is amended so that these definitions do not apply for the purposes of sections 94 to 94.3, except where the definition applies for the purposes of the Act as a whole because of subsection 248(1). This amendment applies to taxation years that begin after 2000.

As set out below, various definitions in subsection 95(1) are also being amended.

"controlled foreign affiliate"

The income for a taxation year of a taxpayer resident in Canada includes, pursuant to subsection 91(1) of the Act, a specified percentage of the foreign accrual property income (FAPI) of any controlled foreign affiliate of the taxpayer. In order to eliminate overlap between the FAPI rules and the rules for foreign investment entities in sections 94.1 and 94.2, the latter rules do not apply in respect of a taxpayer's interest in a controlled foreign affiliate of a taxpayer resident in Canada. An election is provided under new subsection 94.1(12) under which a foreign affiliate of a taxpayer can be treated as controlled foreign affiliate.

The definition "controlled foreign affiliate" is amended to make a cross-reference to foreign affiliates that are deemed by subsection 94.1(12) to be controlled foreign affiliates. Given the wording in subsection 94.1(12), this reference is not technically necessary but is meant to serve as a useful clarification of the potential application of subsection 94.1(12).

This amendment applies after 2000.

"foreign accrual property income"

The FAPI of a controlled foreign affiliate of a taxpayer resident in Canada is allocated to the taxpayer in accordance with subsection 91(1) of the Act. Under its definition in subsection 95(1), FAPI includes certain amounts that would be included in the affiliate's income under existing subsection 94.1(1) if that subsection were read in the manner specified in the description of C of the definition.

Existing section 94.1 is being repealed. Accordingly, the description of C in the definition "foreign accrual property income" is also repealed. There are, however, special rules in new paragraph 95(2)(*g*.2) with regard to the application of sections 94.1 to 94.3 for the purposes of computing FAPI.

This amendment applies to taxation years of controlled foreign affiliates that begin after 2000.

"investment business"

"Investment business" of a foreign affiliate means a business carried on by the foreign affiliate the principal purpose of which is to derive income from property. However, an arm's length business carried on by a foreign bank, trust company, credit union, insurance corporation or securities trader is excluded from the definition "investment business" where the business is regulated in the country in which the business is principally carried on and a 5-employee test is satisfied.

The definition is amended to clarify that the regulation of the business must be under the laws of the country. This language corresponds to a similar definition of the same expression in new subsection 94.1(1).

"relevant tax factor"

The existing definition "relevant tax factor" provides that the "relevant tax factor" for an individual is 2 and for a corporation is the reciprocal of the basic corporate tax rate (i.e., 1/.38, or 2.63).

Under new section 94.1, the "relevant tax factor" is relevant in determining the extent to which relief is provided for investors in foreign investment entities in respect of income or profits taxes payable by those entities. (See, in this regard, subsection 94.1(8).) Partnerships may hold interests in such entities, in which case it may become necessary to compute a relevant tax factor in respect of a partnership.

The definition "relevant tax factor" is amended so that the relevant tax factor for a partnership is 2, except where its members consist entirely of corporations resident in Canada and non-resident persons. In the latter case, the "relevant tax factor" is 2.63.

This amendment applies after 2000.

ITA
95(2)

Subsection 95(2) of the Act provides rules for determining the income of a foreign affiliate of a taxpayer resident in Canada. These rules apply for the purposes of sections 90 to 95.

The rules in new paragraph 95(2)(*g*.2) set out the manner in which sections 94.1 to 94.3 apply for the purpose of computing the FAPI of a particular foreign affiliate of a Canadian taxpayer for a particular taxation year of the affiliate:

- The exemption in the definition "exempt interest" for controlled foreign affiliates is treated as if it referred only to controlled foreign affiliates of the Canadian taxpayer (not of the particular affiliate).[36]

- The measures in sections 94.1 and 94.2 that would otherwise restrict their application to residents in Canada are ignored.[37]

- The Canadian taxpayer, rather than the particular affiliate, claims deductions relevant in determining the particular affiliate's income allocation or loss allocation in respect of a participating interest in a foreign investment entity held by the particular affiliate.[38] These claims are only relevant for taxation years of the particular affiliate that begin after 2000, once the particular affiliate holds an interest in the foreign investment entity and is a controlled foreign affiliate of the Canadian taxpayer.[39]

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[36] Subparagraph 95(2)(*g*.2)(i).

[37] Subparagraph 95(2)(*g*.2)(ii), (x) and (xi).

- The exclusion of dividends under paragraph 94.1(5)A(*g*) applies only where the Canadian taxpayer is resident in Canada, in connection with dividends received by the particular affiliate from foreign affiliates of the Canadian taxpayer (not of the particular affiliate) in which the Canadian taxpayer (not the particular affiliate) has a qualifying interest (determined under paragraph 95(2)(*m*)).[40]

- In the event that the particular affiliate has a participating interest in a particular foreign investment entity and the particular entity has a participating interest in another non-resident entity, the application of sections 94.1 and 94.2 to the particular entity is determined as if the exclusion from the application of those sections for controlled foreign affiliates referred to in paragraph (*a*) of the definition "exempt interest" in subsection 94.1(1) were for controlled foreign affiliates of the Canadian taxpayer (not controlled foreign affiliates of the particular entity).[41] This rule applies instead of the rule in paragraph 94.1(5)A(*i*).[42]

- The Canadian taxpayer (rather than the particular affiliate) is permitted to make an election under subsection 94.1(4) or subparagraph 94.2(4)(*a*)D(i) in connection with the particular affiliate's participating interests in foreign investment entities.[43]

- The particular affiliate's deferral amount determined under paragraph 94.2(1)(*b*) does not include the portion of the amount that can reasonably be considered to have accrued during the period that the particular affiliate was not a foreign affiliate of the Canadian taxpayer and certain other specified persons.[44]

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[38] Subparagraphs 95(2)(*g*.2)(iii) and (iv).

[39] Clause 95(2)(*g*.2)(viii)(B).

[40] Subparagraphs 95(2)(*g*.2)(v) and (vi).

[41] Clause 95(2)(*g*.2)(viii)(A).

[42] Subparagraph 95(2)(*g*.2)(vii).

[43] Subparagraph 95(2)(*g*.2)(ix).

This amendment applies to taxation years that begin after 2000.

Clause 13

ITA
96(1.9)

New subsection 96(1.9) of the Act is relevant where an "exempt taxpayer" (in general, an individual who has been resident in Canada for fewer than 60 months) is a member of a partnership and the partnership invests in a foreign investment entity. In these circumstances, the exempt taxpayer's share of the partnership's income or loss is computed without regard to new sections 94.1 and 94.2. For further details on the application of section 94.2 to partnerships, see the commentary on new subsections 94.2(6) to (8).

This amendment applies to fiscal periods of partnerships that begin after 2000.

ITA
96(3)

Subsection 96(3) of the Act provides rules that apply if a member of a partnership makes an election under certain provisions of the Act for a purpose that is relevant to the computation of the member's income from the partnership. In such a case, the election will be valid only if it is made on behalf of all the members of the partnership and the member had authority to act for the partnership. Subsection 96(3) is amended so that it applies for the purposes of elections under

- new paragraph 94.1(5)A(*c*) (election by taxpayer to use discretionary deductions on behalf of FIE);
- new subsection 94.1(12) (election to treat foreign affiliate as controlled foreign affiliate);

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[44] Subparagraph 95(2)(*g*.2)(xii).

- new subsection 94.1(4) (election to have accrual regime for foreign investment entities apply);
- new subparagraph 94.2(4)(*a*)D(i) (election to recognize positive deferral amount before year of disposition); and
- new paragraph 95(2)(*g*.2) (elections and designations for the purposes of computing foreign accrual property income).

This amendment applies to fiscal periods of partnerships that begin after 2000.

ITA
96(9)

Subsection 96(8) of the Act provides rules that apply where, at a particular time, a Canadian resident becomes a member of a partnership, or a person who is a member of such a partnership becomes a resident of Canada. Where, immediately before the particular time no member of the partnership was resident in Canada, these rules apply in computing the income of the partnership for fiscal periods ending after the particular time. In general terms, the rules in subsection 96(8) are designed to prevent losses accrued while a partnership had no Canadian resident partners from being used to reduce Canadian income tax liabilities.

Subsection 96(9) provides that, where one of the main reasons that there is a member of the partnership who is resident in Canada is to avoid the application of subsection 96(8), that member will, for the purpose of applying subsection 96(8), be considered not to be resident in Canada.

Subsection 96(9) is amended to provide an explicit look-through rule for the purposes of subsection 96(8) so that members of partnerships may be identified through one or more tiers of partnerships which are members of other partnerships. Amended subsection 96(9) is consistent with new subsection 94.2(8).

This amendment applies to partnership fiscal periods that begin after **ANNOUNCEMENT DATE**.

Clause 14

ITA
104(1.1)

Proposed subsection 104(1.1) of the Act was one of the measures contained in a detailed Notice of Ways and Means Motion tabled on June 5, 2000.

Proposed subsection 104(1.1) of the Act applies for the purpose of identifying beneficiaries under a trust for the purpose of subsection 104(1), as well as for the purposes of proposed subparagraph 73(1.02)(*b*)(ii) and proposed paragraph 107.4(1)(*e*). Those provisions use the expression "beneficiary". Proposed subsection 104(1.1) deems a person or partnership not to be a "beneficiary" under a trust at a particular time for the purposes of those various provisions where the person or partnership is beneficially interested in the trust at the particular time solely because of a contingent right described in subsection 104(1.1).

It is proposed that subsection 104(1.1) be amended to also apply for the purpose of paragraph (*b*) of the definition "resident beneficiary" in new subsection 94(1), so that contingent rights described in subsection 104(1.1) will not result in a person being treated as a "resident beneficiary". For more detail on the implications of status as a resident beneficiary, see new subsection 94(3).

This amendment applies to trust taxation years that begin after 2000.

ITA
104(4.1)

New subsection 104(4.1) of the Act provides that, for the purposes of the 21-year deemed disposition rule in subsection 104(4), a property's status as capital property is determined without reference to new subparagraph 39(1)(*a*)(ii.3) and new section 94.2. The latter provisions have the effect of providing that interests in foreign investment entities to which subsection 94.2 applies are not classified as capital property. In the event that such an interest is deemed to have been disposed of because of the application of subsection 104(4), there is a recognition of the "deferral amount" pursuant to subsection 94.2(4).

This amendment applies to trust taxation years that begin after 2000.

ITA
104(6)

Subsection 104(6) of the Act generally permits a trust to deduct, in computing income for a taxation year, any income payable to a beneficiary under the trust.

Subsection 104(6) is amended so that it is expressly subject to subsection 104(7) and new subsection 104(7.01).

This amendment applies to trust taxation years that begin after 2000.

ITA
104(7.01)

New subsection 104(7.01) of the Act restricts the amount that a trust, that is deemed by subsection 94(3) to be resident in Canada, can deduct in computing its income in the event that the trust has Canadian-source income and makes distributions to beneficiaries not resident in Canada.

Subsection 104(7.01) effectively acts as a proxy for taxes under Parts XII.2 and XIII. Trusts to which new subsection 94(3) applies are not subject to Part XII.2 because of an existing exemption for non-resident trusts in Part XII.2. They are also exempt from collecting Part XIII tax because they are not treated as resident in Canada for this purpose. Further, because of new subparagraph 94(3)(*a*)(iii), they are exempt from Part XIII tax on payments made to them. (The latter Part XIII exemption is new. Existing subparagraph 94(1)(*c*)(ii) allows a tax credit to be claimed under section 126 in connection with Part XIII tax.)

More specifically, the amount by which the maximum deduction under subsection 104(6) for a taxation year is reduced under subsection 104(7.01) is equal to the lesser of two amounts:

- the total of
    - the trust's "designated income" for the year (as defined in Part XII.2), which essentially consists of taxable capital gains

from taxable Canadian property and income from businesses carried on in Canada, and

  - 50% of all amounts paid or credited in the year to the trust that would, disregarding express provisions to the contrary in the Act, be subject to Part XIII tax; and

- the portion of the maximum deduction under subsection 104(6) that is attributable to amounts that become payable in the year (determined with reference to subsection 104(24)) to non-resident persons and to partnerships (other than Canadian partnerships, referred to in section 102).

The example below illustrates the operation of new subsection 104(7.01).

Example

1. Trust X is an offshore trust established by Stefan, a long-term resident of Canada. The primary beneficiaries under the trust are Linda (a resident of Canada) and Bart (a resident of the United States).
2. Trust X receives $400 of dividends from a taxable Canadian corporation and has $1,200 of other income.
3. Trust income of $1,250 for 2001 is made payable to Bart. The remaining $350 is made payable to Linda.
4. Trust X is assumed to have designated $400 of dividends under subsection 104(19).

Results

1. Trust X is deemed by new subsection 94(3) to be resident in Canada for the purposes of computing its income.
2. Before taking into account subsection 104(6), Trust X's income is $1,600. Note, in this regard, that the dividends are included in

computing the trust's income because of a proposed amendment to subsection 104(19).[45]

3. Before taking into account new subsection 104(7.01), the maximum deduction under subsection 104(6) is also $1,600.

4. Because of subsection 104(7.01), the maximum deduction under subsection 104(6) is reduced to $1,400 (i.e., $1,600 minus the lesser of: (50% x $400) and ($1,600 - $1,250)).

5. Assuming that the trust claims a deduction of $1,400, the trust would consequently have income of $200. If a tax rate of 50% were assumed, the trust would be liable for Canadian income tax of $100. (Note: The trust is expressly exempted from a Part XIII tax liability under new subparagraph 94(3)(*a*)(iii).) Disregarding this exemption, Part XIII tax liability would also have been $100 (i.e., 25% of $400).

New subsection 104(7.01) applies to trust taxation years that begin after 2000.

ITA
104(21.3)

Subsection 104(21.3) of the Act defines the expression "net taxable capital gains". The expression is used in subsections 104(21) and (21.2), which permit a trust to flow its taxable capital gains realized in a year through to a beneficiary who has received a portion of the trust's income for the year. The trust can flow through its taxable capital gains to beneficiaries only to the extent of its net taxable capital gains for the year.

Under subsection 104(21.3), the net taxable capital gains of a trust for a taxation year equals the amount, if any, by which its total taxable capital gains for the year exceeds the total of two amounts:

- its total allowable capital losses for the year, and

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[45] This refers to an amendment to subsection 104(19) contained in a detailed Notice of Ways and Means Motion tabled on June 5, 2000.

- the amount deducted by it under paragraph 111(1)(*b*) in computing its taxable income for the year (i.e., deduction of carried-over net capital losses for years preceding and the 3 years immediately following the year).

Subsection 104(21.3) is amended so that allowable business investment losses (ABILs) are disregarded for the purpose of the first of the two amounts. Accordingly, ABILs will not result in a reduction of taxable capital gains that may be flowed through to beneficiaries under trusts and against which allowable capital losses can be claimed.

This amendment applies to trust taxation years that begin after 2000.

ITA
104(24)

The determination of when an amount becomes payable in a taxation year is relevant for a number of purposes, including the determination of the amount deductible under subsection 104(6) of the Act. Under subsection 104(24), an amount (e.g., income payable to a beneficiary) is deemed not to have become payable in the year to a beneficiary unless it was paid in the year to the beneficiary or the beneficiary was entitled in the year to enforce payment of the amount.

Subsection 104(24) is amended so that it also applies for the purpose of new subsection 104(7.01), which is described in the commentary above.

This amendment applies to trust taxation years that begin after 2000.

Clause 15

ITA
108(3)

Subsection 108(3) of the Act provides that, for the purposes of the definition "income interest" in subsection 108(1), the income of a trust is its income computed without reference to the provisions of the Act. Amendments to subsection 108(3) were contained in a detailed Notice of Ways and Means Motion tabled on June 5, 2000.

It is proposed to further amend subsection 108(3) so that the rule described above also applies for the purposes of the definition "exempt foreign trust" in new subsection 94(1).

This amendment applies to taxation years that begin after 2000.

Clause 16

ITA
113

Subsection 113(1) of the Act permits a resident corporation to deduct specified amounts in respect of dividends received from a foreign affiliate out of the exempt, taxable and pre-acquisition surplus of the foreign affiliate. The amounts so deductible are determined largely with reference to Part LIX of the Regulations. The deductions under paragraphs 113(1)(*b*) and (*c*) with regard to dividends out of taxable surplus are also determined with reference to the resident corporation's "relevant tax factor".

Subsection 113(1) is amended to explicitly link the "relevant tax factor" to the resident corporation receiving the dividends and the taxation year in which the dividends are received. This is consistent with the more explicit definition of "relevant tax factor" described above in the commentary on subsection 95(1).

This amendment applies after 2000.

Clause 17

ITA
114

Section 114 of the Act provides rules for computing the taxable income of an individual who is resident in Canada for a period or periods in a taxation year, and is non-resident for the rest of the year. Amendments to section 114 were contained in a detailed Notice of Ways and Means Motion tabled on June 5, 2000.

Section 114 is amended so that it is subject to paragraph 94.2(5)(*c*), a rule that applies in connection with interests in foreign investment entities that are subject to the mark-to-market regime under section 94.2. Paragraph 94.2(5)(*c*) is, however, only relevant to individuals who cease to be, and later become, resident in Canada in the same taxation year. For further detail, see the commentary on new subsection 94.2(5).

This amendment applies to the 2001 and subsequent taxation years.

Clause 18

ITA
122(2)(*d*.1)

Subsection 122(1) of the Act provides that, instead of graduated income tax rates, *inter vivos* trusts are generally subject to top marginal rates of income tax on their undistributed income. Subsection 122(2) permits graduated income tax rates for certain *inter vivos* trusts established before June 18, 1971. One of the conditions for an *inter vivos* trust continuing to qualify for graduated income tax rates is that it not receive any gifts after June 18, 1971.

Paragraph 122(2)(*d*.1) is introduced so that the graduated income tax rates cease to apply to a trust in the event that, after **ANNOUNCEMENT DATE**, a "contribution" is made to the trust. The expression "contribution" is defined in new section 94.

This amendment applies to taxation years that begin after 2000.

Clause 19

ITA
149(10)(*c*)

Subsection 149(10) of the Act applies where, at a particular time, a corporation becomes or ceases to be exempt from tax under Part I on its taxable income (otherwise than by reason of the exemption for certain insurers in paragraph 149(1)(*t*)). A new taxation year is considered to start at the particular time and the corporation's properties are deemed to have been disposed of at fair market value and reacquired at the particular time for the same amount. Paragraph 149(10)(*c*) provides that the corporation is, for specified purposes in the Act, treated as a new corporation. One of the specified purposes is with regard to the investment tax credit regime set out in subsections 127(5) to (26).

Paragraph 149(10)(*c*) is amended to make a reference to additional rules for the investment tax credit that are set out in subsections 127(27) to (35). This amendment is strictly consequential on the earlier enactment of these subsections.

Paragraph 149(10)(*c*) is also amended so that it also applies for the purposes of sections 94.1 to 94.3 (foreign investment entities). For example, a corporation's "deferral amount" (as defined in new subsection 94.2(1)) in respect of any interest it holds in a foreign investment entity is determined without reference to taxation years that occurred before the corporation's change of status. This will typically result in a nil deferral amount for the corporation.

These amendments apply to corporations that, after 2000, become or cease to be exempt from tax on their taxable income under Part I of the Act.

Clauses 20 and 21

ITA
162 and 163

Subsection 162 and 163 of the Act impose penalties for infractions such as failing to provide certain information on a return, failing to file a return for a taxation year, and making false statements on a return.

ITA
162(10.1) and (10.11)

Subsection 162(10.1) of the Act imposes a penalty on any person or partnership that is more than 24 months late in filing an information return that the person or partnership was required to file under any of sections 233.1 to 233.4. (This penalty applies in addition to the penalties imposed under subsections 162(7) and (10)).

The penalty imposed under subsection 162(10.1) with respect to a particular information return is equal to a specified amount less the amount of the penalties imposed under subsections 162(7) and (10) with respect to the return. The specified amount with respect to an information return for a trust required to be filed by a person or partnership under section 233.2 is equal to 5% of the total fair market value of any property transferred or loaned to the trust that, if no other loan or transfer were taken into account, would have imposed an obligation on the person or partnership to file the return.

Subsection 162(10.1) is amended as a consequence of amendments made to section 233.2, by changing the manner in which the specified amount is determined. The specified amount is now to be determined with reference to the fair market value of "contributions" made by the person or partnership to the trust.

New subsection 162(10.11) provides that, for the purpose of the calculation in subsection 162(10.1), the definitions and rules in subsections 94(1) and (2) generally apply. Subsection 162(10.11) is similar to amended subsection 233.2(2), described in greater detail in the commentary below.

This amendment applies to returns in respect of taxation years that begin after 2000.

ITA
162(10.3), 162(10.4), 163(2.6) and 163(2.91)

Existing paragraph 94(1)(*d*) of the Act provides for non-resident trusts to be treated as foreign affiliates, but is being repealed as a consequence of the introduction of new rules for non-resident trusts in section 94. Subsections 162(10.3) and (10.4) are rules affecting the calculation of penalty tax in respect of a person's or partnership's failure to file a return in respect of a foreign affiliate.

Subsections 163(2.6) and (2.91) are similar provisions that affect the calculation of penalty tax in respect of false statements and omissions in such a return.

Subsections 162(10.3) and 163(2.6) are amended to reflect the changes to section 94 under which non-resident trusts are no longer treated as foreign affiliates. Subsections 162(10.4) and 163(2.91) are repealed for the same reason.

These amendments apply to returns in respect of taxation years that begin after 2000.

ITA
163(2.4)(*b*) and (2.41)

Subsection 163(2.4) of the Act imposes a penalty on any person or partnership that, knowingly or under circumstances amounting to gross negligence, has made or has participated in, assented to, or acquiesced in, the making of a false statement or omission in a return required to be filed under any of sections 233.1 to 233.6. The penalty under paragraph 163(2.4)(*b*) relates to a return required to be filed under section 233.2. The existing penalty is the greater of $24,000 and 5% of the total fair market value of the property that the person or partnership loaned or transferred to the trust that gave rise to the obligation to file.

Paragraph 163(2.4)(*b*) is amended as a consequence of changes made to the non-resident trust rules in section 94 and the annual reporting requirement in respect of non-resident trusts under section 233.2. Under amended section 233.2, a person is subject to the annual reporting requirement where a "contribution" is made to the trust by the person.

Accordingly, amended paragraph 163(2.4)(*b*) provides for a penalty for a person equal the greater of $24,000 and 5% of a specified amount in respect of the return. The specified amount for a person is essentially equal to 5% of the fair market value of "contributions" made by the person. The specified amount is calculated in the same way as the specified amount under amended subsection 162(10.1) in respect of late-filed returns. Under new subsection 163(2.41), the definitions and rules in subsections 94(1) and (2) generally apply. Subsection 163(2.41) is similar to amended subsection 233.2(2), described in greater detail in the commentary below.

This amendment applies to returns in respect of taxation years that begin after 2000.

Clause 22

ITA
233.2

Existing section 233.2 of the Act requires certain persons who have made transfers or loans to a "specified foreign trust", or to a non-resident corporation that is a controlled foreign affiliate of such a trust, to file annual information returns with respect to the trust. A "specified foreign trust", as defined in subsection 233.2, includes a trust with a "specified beneficiary" resident in Canada. As defined in subsection 233.2(1), a "specified beneficiary" is generally any beneficiary under the trust with the exception of persons listed in subparagraphs (*a*)(i) to (x) of the definition. For a return to be required to be filed as a consequence of a transfer or loan, it is necessary to have a "non-arm's length indicator", as set out in subsection 233.2(2), apply in respect of the transfer or loan. One of the cases where a "non-arm's length indicator" applies in respect of a transfer to a trust is where the transferor is a "specified beneficiary" under the trust. Subsection 233.2(3) provides a look-through rule so that where a partnership transfers property, it is considered to have been transferred by members of the partnership.

New section 94 sets out new rules governing the taxation of non-resident trusts. In order to be consistent with the new rules:

- the definitions "specified beneficiary" and "specified foreign trust" in section 233.2 are repealed,

- there is no longer a requirement for a "non-arm's length indicator", so the existing rule in subsection 233.2(2) is repealed,

- except as described below, the definitions and rules of application in section 94 apply because of amended subsection 233.2(2), and

- there is no longer a requirement for an explicit look-through rule for partnerships in section 233.2, given that the rule in paragraph 94(2)(*m*) applies because of amended subsection 233.2(2). Consequently, subsection 233.2(3) is repealed.

Under amended subsection 233.2(4), reporting will generally be required for a taxation year whenever a "contribution" has been made by a person resident in Canada to a non-resident trust at or before the end of the year. Because of amended subsection 233.2(2), the expression "contribution" generally carries the same meaning as in new section 94 with most of the same exceptions for "arm's length transfers" contained in the definition of that expression in subsection 94(1). However, the exception contained in subparagraph (*a*)(v) of that definition (transfers or loans not undertaken to allow for the conferral of benefits on non-arm's length persons) does not give rise to an exception to the obligations for reporting under subsection 233.2(4). It should be noted that amended subsection 233.2(2) also applies for the purpose of new paragraph 233.5(*c*.1).

New subparagraph 233.2(4)(*b*)(ii) sets out a list of persons for whom reporting obligations are not imposed. This list is consistent with the list of beneficiaries who are not treated as "specified beneficiaries" under the existing rules in section 233.2.

Amended subsection 233.2(4) of the Act also exempts contributors from filing information returns with regard to trusts described in paragraphs (*c*) to (*i*) of the new definition "exempt foreign trust" in subsection 94(1). For more detail in this regard, see the commentary on that definition.

These amendments apply to returns in respect of taxation years that begin after 2000.

ITA
233.2(4.1)

New subsection 94(3) of the Act provides that, where a non-resident trust has a resident contributor or resident beneficiary at the end of the trust's taxation year, the trust is generally taxed on its income in Canada for the year as if the trust were resident in Canada. However, subsection 94(3) applies only to arrangements that are considered to be trusts for Canadian income tax purposes. In some cases, there may be doubt as to whether a given arrangement is a trust for Canadian income tax purposes.

New subsection 233.2(4.1), in combination with new subsection 233.2(4), imposes a filing obligation on contributors to certain entities or arrangements in respect of which reporting is not otherwise required. One of the key objectives of subsection 233.2(4.1) is to ensure that claims that section 94 does not apply can be reviewed by the CCRA.

More specifically, new subsection 233.2(4.1) applies where property has, directly or indirectly, been transferred or loaned by a person to be held

- under an arrangement governed by laws that are not laws of Canada or a province, or
- by a non-resident entity (as defined in subsection 94.1(1)).

The person must, where certain additional conditions are satisfied, file the information return referred to in amended subsection 233.2(4).

New subsection 233.2(4.1) provides that, except as the Minister of National Revenue otherwise permits in writing, the person has obligations under amended subsection 233.2(4) if all of the following conditions are satisfied:

- the transfer or loan would not be an arm's length transfer (within the meaning assigned by the definition "arm's length transfer" in subsection 94(1) if that definition were read without reference to the words "in respect of a trust" and to subparagraph (*a*)(v) of that definition);
- the transfer or loan is not solely in exchange for property that would be described in paragraphs (*a*) to (*i*) of the definition "specified foreign property" in subsection 233.3(1) if that definition were read without reference to paragraphs (*j*) to (*q*) of that definition;
- the entity or arrangement is not a trust in respect of which the person would, without reference to subsection 233.2(4.1) and the explicit exemptions for filing returns contained in subsection 233.2(4), be required to file an information return for a taxation year that includes that time; and

- the entity or arrangement is not an exempt foreign trust (as defined in subsection 94(1)) or an exempt trust (as defined in subsection 233.2(1)).

Where the above conditions are satisfied, the person's obligations under subsection 233.2(4) and related provisions are determined as if:

- the transfer were a contribution to which paragraph 233.2(4)(*a*) applied;

- the entity or arrangement were a trust not resident in Canada throughout the calendar year that includes the time of the transfer or loan; and

- the taxation year of the entity or arrangement were that calendar year.

These amendments apply to returns in respect of taxation years that begin after 2000.

Clause 23

ITA
233.3

Section 233.3 of the Act provides reporting requirements in respect of foreign property. In general terms, it provides that certain taxpayers resident in Canada and certain partnerships must file an information return with respect to their "specified foreign property" if the total cost amount of such property exceeds $100,000. For this purpose, "specified foreign property" (as defined in subsection 233.3(1)) includes an interest in a non-resident trust or a trust that would be non-resident were it not for section 94. It does not include an interest in a non-resident trust that was not acquired for consideration by the person or partnership.

Paragraph (*d*) of the definition "specified foreign property" is amended by changing a cross-reference to section 94 to a cross-reference to new subparagraph 94(3)(*a*)(ii). This amendment is strictly consequential on amendments to section 94. As a consequence, interests in trusts deemed to be resident of Canada because of section 94 are "specified foreign property" unless otherwise expressly excluded.

Paragraph (*d*.1) of the definition is introduced so that specified foreign property includes an interest in an insurance policy issued by a non-resident insurer, if the mark-to-market regime in section 94.2 applies in respect of the interest. For further detail in this regard, see the commentary on new subsection 94.2(10).

Paragraph (*l*) of the definition is repealed to eliminate a reference to trusts that are treated as foreign affiliates. This reference is no longer necessary in light of new subsection 94(1), under which non-resident trusts are no longer treated as foreign affiliates.

Paragraph (*m*) of the definition is amended so that the exclusion for non-resident trusts that applies with regard to interests not acquired for consideration also applies to trusts that are deemed to be resident in Canada by subsection 94(3). This amendment is made for consistency.

These amendments generally apply to interests in a trust held in taxation years of the trust that begin after 2000. However, new paragraph (*d*.1) applies in respect of returns required to be filed for taxation years that begin after 2001, in order to be consistent with new subsection 94.2(10).

Clause 24

ITA
233.4(1) and (2)

Section 233.4 of the Act provides reporting requirements in respect of foreign affiliates. In general terms, it provides that taxpayers resident in Canada (or certain partnerships) of which a non-resident corporation or non-resident trust is a foreign affiliate must file an information return in respect of the affiliate.

Subsections 233.4(1) and (2) are amended to eliminate references to foreign affiliates that are non-resident trusts. These references are no longer necessary in light of new subsection 94(1), under which non-resident trusts are no longer treated as foreign affiliates.

These amendments apply to taxation years and fiscal periods that begin after 2000.

Clause 25

ITA
233.5

Section 233.5 of the Act provides that, where specified conditions set out in paragraphs 233.5 (*a*) to (*d*) are met, information required in a return filed under section 233.2 or 233.4 does not include information that is not available to the person or partnership required to file the return. In the case of a return required to be filed by a person or partnership under section 233.2, paragraph 233.5(*c*) provides that it must be reasonable for the person or partnership to expect, at the time of each transaction entered into by the person or partnership after March 5, 1996 that either gives rise to the requirement to file the return or that affects the information to be reported in the return, that sufficient information would be available to the person or partnership to comply with section 233.2.

Paragraph 233.5(*c*) is amended so that it only applies in connection with transactions entered into before [**ANNOUNCEMENT DATE + 1**]. In connection with trust returns required to be filed for trust taxation years that begin after 2000, it must be reasonable for the person or partnership to expect that sufficient information would have been available to the person or partnership to comply with section 233.2 if the proposed amendments to section 94 were not taken into account.

Paragraph 223.5(*c*) is also amended so that it does not apply to returns required to be filed under section 233.4. It is replaced in this respect by new paragraph 233.5(*c*.2), without any change in the specified conditions for such returns.

Paragraph 233.5(*c*.1) is introduced in connection with returns required to be filed under section 233.2 by a person or partnership for a taxation year of the trust that begins after 2000. Where "contributions" (determined with reference to subsection 233.2(2), referred to in the commentary above) are made after **ANNOUNCEMENT DATE**, relief under section 233.5 is available only if it was reasonable for the person or partnership to expect, at the time of each such contribution that either gives rise to the requirement to file the return or that affects the information to be reported in the return, that sufficient information would be available to the person or partnership to comply with section 233.2.

Clause 26

ITA
248(1)
"cost amount"

Subsection 248(1) of the Act defines "cost amount", which is used throughout the Act, particularly in provisions relating to the transfer of properties to and from corporations, trusts and partnerships.

New paragraph (*c*.2) of the definition "cost amount" provides that, where a cost of property to a taxpayer is determined as of any time under new subsection 94.2(12), that cost is also the "cost amount", under subsection 248(1), of the property to the taxpayer at that time.

This amendment applies after 2000.

ITA
248(1)
"inventory"

A taxpayer's "inventory" is generally described in subsection 248(1) of the Act as a description of property the cost or value of which is relevant in computing a taxpayer's income from a business for a taxation year. Rules for "inventory" in section 10 and elsewhere in the Act affect the calculation of a taxpayer's income from business.

The definition "inventory" is amended to exclude descriptions of property to the disposition of which subsection 94.2(3) applies.

This amendment applies to fiscal periods that begin after 2000.

ITA
248(1)
"foreign accrual property income"

The definition "foreign accrual property income" is introduced so that the definition of this expression in section 95 of the Act applies for the purposes of the Act.

This amendment applies after 2000.

ITA
248(1)
"non-discretionary trust"

The definition "non-discretionary trust" is introduced so that the existing definition of the expression in subsection 17(15) applies for the purposes of the Act. The expression is used in the definition "foreign investment entity" in new subsection 94.1(1).

This amendment applies after 2000.